No. 8881

In the United States

Circuit Court of Appeals

For the Ninth Circuit

INVESTORS SYNDICATE, PORTLAND TRUST AND SAVINGS BANK, Trustee, and METROPOLITAN LIFE INSURANCE COMPANY,

Appellants,

vs.

LLOYD R. SMITH, Trustee in the Matter of Guaranty Trust Company, a corporation, and National Investment Company, a corporation, its affiliate, Bankrupts, GESINA KING, HELEN WINSOR JOHNSON, BERT WHY and ELSA STRATHMAN, MRS. GOW WHY, CONRAD BAURIEDEL, IDA ISABELL NEILSON, GEORGE J. and EMMA C. FOURIER, JAMES T. JONES and LOUIS KNUTSON, and RALPH A. COAN and S. J. BISCHOFF,

Appellees.

BRIEF OF APPELLEES

Upon Appeal from the District Court of the United States for the District of Oregon.

STEVENS-NESS LAW PUB CO., PORTLAND 83426

STATEMENT OF THE CASE

The relevant facts are as follows:

Guaranty Trust Company (and National Investment Company, its affiliate) were the owners of a large number of real properties, encumbered and unencumbered. An involuntary petition in bankruptcy was filed against the Company in January, 1934. Bankrupt purposely "stalled" adjudication until Sec. 77B was enacted when it filed an answer seeking reorganization.

The reorganization proceeding resulted in an order of liquidation which constituted an "Adjudication". Trustees were appointed, order of reference made and the estate is being administered in bankruptcy.

The trustee took possession of the assets consisting of many parcels of real property, encumbered and unencumbered, mortgages, securities and personal property (including properties upon which aplants held mortgages).

The trustees collected rents from these properties and appellants, by the petitions now under consideration, seek to have turned over to them the rents collected from properties upon which they hold mortgages.

The Investors Syndicate's five mortgages were all executed prior to the 1927 Amendment to Section 5-112 Oregon Code.

The Metropolitan Insurance Company held one mortgage made subsequent to the 1927 Amendment.

Investors Syndicate and Metropolitan Life Ins. Co. did not, prior to the filing of the bankruptcy petition, commence any foreclosure proceeding or obtain a receiver, nor did they collect any rents, nor did they obtain possession of the property covered by their mortgage. The first attempt to obtain the rents was made long after bankruptcy when they petitioned for leave to institute foreclosure proceedings (in other courts).

The Portland Trust & Savings Bank was the holder of two mortgages on two parcels of real property made subsequent to the aforesaid Amendment. It commenced suit to foreclose these mortgages in the state court prior to the filing of the bankruptcy petition, prayed for the appointment of a receiver. The application was denied, but the Court made orders directing the owner to file monthly statements showing receipts and disbursements and requiring the net revenues to be deposited with the Clerk of the state court. The orders did not require surrender and the owner remained in possession.

None of the appellants ever petitioned the Bankruptcy Court to turn over possession of the properties to them, or that the trustee should abandon the mortgaged properties, or for the sale of the mortgaged properties free of liens with permission to bid the amount of their mortgage debt at such sale, or for the extension of the trusteeship for their benefit.

They did not seek to have their mortgage liens established and foreclosed in the bankruptcy proceeding, or have the value of their security determined and the extent of deficiency, if any, ascertained in the manner required by Section 57 (h) (11 U.S.C.A. 93 (h)) Bankruptcy Act. On the contrary they sought and were granted permission to foreclose their mortgages in other courts.

The **appellant mortgagees appeared specially in the proceedings and refused to submit to the jurisdiction of the Bankruptcy Court** (R. 6).

The order requiring the trustees to keep separate accounts (R. 8) was not made for the benefit of appellants and they are not referred to therein by name or description. The order is not limited to properties covered by appellants' mortgages or any mortgages but includes all properties, encumbered or unencumbered. **The order was not made on petition by or on behalf of appellants.** The order does not require that the monies so collected be kept in separate funds. It deals with bookkeeping only.

We deem it necessary to focus attention at this point upon the terms of the order because appellants, throughout their brief, erroneously assert that this order required the maintenance of separate accounts for the benefit of these mortgagees, and upon that erroneous assertion, they predicate the argument that this order constitutes a sequestration of the rents for their benefit.

The same erroneous assertion is made with respect to the accounts filed by the trustees. It is asserted that the trustees filed accounts showing segregation of the rents derived from the mortgaged properties. This is only partially true. The trustees filed separate accounts of receipts and disburse ments from **all** properties, **encumbered or unencumbered.**

Long after the making of the order by Judge McNary for the keeping of separate accounts, each of the appellants petitioned the Court that the rents be segregated for their benefit, which was clearly a recognition that the order theretofore made was not a sequestration for their benefit. **These are the petitions which resulted in the order now under review.**

The Special Master, to whom these petitions were referred, recommended that the rents be paid over to the mortgagees. Upon exceptions to the report, District Court Judge James Alger Fee sustained the exceptions and denied appellants' petitions for the rents.

MOTION TO DISMISS THE APPEAL

There is now pending appellee's motions to dismiss the appeals, based upon the ground, among others, that this case is a "proceeding in bankruptcy", and hence, leave to appeal must be granted by this Court and not the District Court.

In **Re: Western Women's Club, 93 Fed. (2d) 189, 192 (9th Cir.)**, this Court held that an application for rents such as in the case at bar is a **"proceeding in bankruptcy"**.

THE ASSIGNMENT OF ERRORS ARE INSUFFICIENT TO PRESENT ANY QUESTION FOR REVIEW.

Each appellant makes two assignments. One is the converse of the other. The three pairs of assignments are alike.

Analysis of assignments numbered 1 and 2 will suffice to present all.

Assignment of Error No. 1, omitting immaterial parts, is as follows:

> "That the Court erred in sustaining the exceptions . . . . . to conclusions of law, numbered 1 to 5, inclusive, of the Special Master's Report . . . . wherein . . . the Master found that the net rentals and income from the . . . . apartments . . . . . in the hands of the trustee . . . . should be held by the trustee for the benefit of the Investors Syndicate . . . ."

The second assignment is clearly a statement of the converse of the first assignment.

All that these assignments say, in effect, is that the Court erred in holding that the trustee in bankruptcy, and not the mortgagees, was entitled to the rents from the mortgaged premises. They do not

point out whether the error lies in (a) lack of any evidence to support the Court's ruling, or (b) the erroneous conception of the law, or (c) the erroneous application of legal principles to the facts in the case, or (d) insufficiency of the findings to support the ruling of the Court, or (e) any other erroneous action.

Rule 11 of this Court provides:

> "In equity cases the assignment shall state, as particularly as may be, in what the findings or decree are alleged to be erroneous."

In **American Surety Company v. Fischer Warehouse Co.**, 88 **Fed.** (2d) 536, 539 (9th Cir.), (1937), this Court said:

> "It is not sufficient that appellant assert generally that the trial court made wrong findings and reached wrong conclusions and then and thereby **invite this court to retry the cause** without indicating to us in such assignments in what respect or for what reason the findings or conclusions are claimed to be in error."
>
> . . . . . .
>
> "What was the erroneous basis used, or the erroneous step made by the court which shows his conclusion was wrong? The court might have erred in reaching his conclusion by considering testimony erroneously admitted; by erroneously excluding evidence; by finding a fact not supported by substantial evidence; by the erroneous application of law; or by some other erroneous action. But we consider alleged errors, and if none are assigned, there are none to consider."

In **Krause vs. Snyder**, 87 **Fed.** (2d) 723, 725 (8th Cir.), the Court held:

> "The purpose of an assignment of error is to point out to the appellate court what action or ruling of the lower court is complained of, and **to indicate in what respect or for what reason the action of the court is claimed to be erroneous.** The party complaining of the action of the lower court 'must lay his finger upon the point of objection and must stand or fall upon the case he made in the court below'."

Assignments similar to those in the case at bar were held insufficient by this court to present any question for review in the following cases:

U. S. vs. Shingle, 91 Fed. (2d) 85 (9th Cir.).
Goldstein vs. United States, 73 Fed. (2d) 804.
United States vs. Alcorn, 80 Fed. (2d) 487-489.
Century Indemnity Co. vs. Nelson, 90 Fed. (2d) 644-646.
O'Brien's Manual of Federal Appellate Procedure (1937), Pages 102-103.

SUMMARY OF APPELLEES' ARGUMENT

1. In Oregon a mortgage on real property is merely a lien. It passes no title, estate or any right whatsoever to the mortgagee until after foreclosure and sale.

Oregon Code, Sec. 5-112.
Teal v. Walker, 111 U.S. 242.
Thomson v. Shirley, 69 Fed. 484 (Dist. of Ore. Affirmed Couper v. Shirley, 75 Fed. 168 (9th Cir.).
McLennan v. Holbrook, 143 Ore. 458.
State ex rel. v. McDonald, 128 Ore. 684.

2. Prior to 1927 Amendment of Sec. 5-112, Oregon Code, provisions in mortgages pledging rents or for

appointment of a receiver were void and unenforcible because against public policy. Mortgagor could not be divested of rents prior to foreclosure and sale, in any manner unless mortgagee obtained peaceful possession.

Oregon Code, Sec. 5-112.
Teal v. Walker, supra.
Thomson v. Shirley, supra.
Couper v. Shirley, supra.
State ex rel. v. McDonald, supra.
McKinney v. Nayberger, 138 Ore. 203.

3. In states like Oregon, mortgagees who have not, prior to bankruptcy, entered into possession, either by consent of the mortgagor or through the appointment of a receiver in foreclosure proceedings, cannot recover rents collected by a trustee in bankruptcy who entered into possession of the mortgaged premises and collected the rents. There can be no substitute for actual possession in the manner provided by the Oregon law.

Re: Hotel St. James Co., 65 Fed. (2d) 82 (9th Cir.).
Lincoln Savings Bank v. Realty Assoc. Sec. Corp., 67 Fed. (2d) 895 (2nd Cir.).
Re: Humeston, 83 Fed. (2d) 187 (2nd Cir.).
Re: McGrory Stores Corp., 73 Fed. (2d) 270 (2nd Cir.).
Dallas Tr. & Sav. Bank v. Ledbetter, 36 Fed. (2d) 221 (5th Cir.).
Wilcox v. Goess, 92 Fed. (2d) 8 (2nd Cir.).
Prudential Ins. Co. v. Liberdar Holding Corp., 74 Fed. (2d) 50 (2nd Cir.).
Re: Berdick, 56 Fed. (2d) 288 (Dist. N.Y.).
Garber v. Barkers Mtg. Co., 27 Fed. (2d) 609.

Bindseil v. Liberty Trust Co., 248 Fed. 112 (3rd Cir.).
Re: Brose, 254 Fed. 664 (2nd Cir.).
Alter v. Clark, 193 Fed. 153 (D.C.), Nev.
Goldman, Beckman & Co. v. Smith, 2 A.B.R. 104.
Annotation, 75 A.L.R. 1526.
Re: Clark Realty Co., 234 Fed. 576 (7th Cir.).
Re: Chase, 133 Fed. 79.
Re: Banner, 149 Fed. 936.
Re: Hasie, 206 Fed. 789.
Re: Sweeney, 212 Fed. 1.
Re: Israelson, 230 Fed. 1000.
Alexander v. Smithe Mach. Co., 143 N.E. 321 (Mass.).

4. Investors Syndicate is not entitled to rents, in any event, because all of its mortgages were made prior to the Amendment (an expository proviso) which has no retroactive effect.

McKinney v. Nayberger, supra.
Detroit Trust Co. v. Lipsitz, 249 N.W. 892 (Mich.).
American Trust Co. v. Michigan T. Co., 248 N.W. 829 (Mich.).
Freedman v. Massachusetts Life Ins. Co., 81 Fed. (2d) 698 (6th Cir.).
Union Guardian T. Co. v. Commercial Realty Co., 251 N.W. 786 (Mich.).

5. Expository legislation cannot be given retrospective effect unless act so declares by clear and positive command.

Libby v. Southern Pac. Co., 109 Ore. 449.
Seton v. Hoyt, 34 Ore. 266.
59 Corpus Juris 692, supported by 10 pages of citation, including many Oregon cases.

6. Void contracts cannot be vitalized by giving retroactive effect to subsequent statutes.

Restatement of the law of Contracts, Vol. 2, p. 1128.
Lewis' Sutherland Statutory Construction, Vol. 1, p. 19; Vol. 2, p. 635; Vol. 2, p. 1219.
Williston on Contracts, Secs. 1683, 1758.
Denny v. McCown, 34 Ore. 47.
Ferguson v. Kaboth, 43 Ore. 414.
Lanning v. Osborne, 82 Fed. 575 (C.C. Cal., Judge Ross).

7. A mortgage pledging future rents does not create any lien **in presenti** but merely a contract for a lien which can ripen into a lien only when the mortgagee has taken possession of the property (in a manner recognized as sufficient by Oregon Law) and has come into possession of the rents.

Re: McCrory Stores Corp., 73 Fed. (2d) 270.
First Joint Stock Land Bank v. Armstrong, 262 N.W. 815.
Lincoln Sav. Bank v. Realty Assoc. Sec. Corp, supra.
Grether v. Nick, 55 A.L.R. 525-532 (Wis.).
Andrew v. Home Savings Bank, 246 N.W. 48.
Sims v. Jamison, 67 Fed. (2d) 409 (9th Cir.).
Flanagan Bank v. Graham, 42 Ore. 403.
Re: West, 128 Fed. 205 (Dist. of Ore.).
Re: Foster, 9 Fed. Cas., p. 523.
No. 4963, Aff'd Case No. 4982.
Women's Hospital v. 67th St. Realty Co., 95 A.L.R. 1031 (N.Y.).
Kooistra v. Gilford, 207 N.W. 399 (Ia.).
Burgess v. Lasby, 9 Pac. (2d) 164 (Mont.).
Southern Trust Co. v. First City Bank & Trust Co., 82 S.W. (2nd) 205.
Alexander v. Smithe Machine Co., 143 N.E. 321 (Mass.).

Norwood v. Romer, 183 N.E. 45 (Ohio).
Re: Pine Tree Lumber Co., 269 Fed. 515 (9th Cir.).
Tolland Co. v. First St. Bank, 35 Pac. (2d) 867 (Cal.).
Annotations—A.L.R., Vol. 4, p. 1410; Vol. 91, p. 1221.

8. Prior to perfection of a lien on rents in the manner indicated above, the rents may be (a) appropriated by the owner to his own use; (b) assigned; (c) seized on attachment or execution; (d) seized by a junior mortgagee who first enters into possession by procuring the appointment of a receiver.

Re: McCrory Stores Corp., supra.
Sullivan v. Rosson, 4 A.L.R. 1400 (N.Y.).
Lincoln Savings Bank v. Realty Assoc., supra.
First Joint Stock Land Bank v. Armstrong, supra.
Bank of America v. Bank of Amador Co., 28 Pac. (2d) 86 (Cal.).
N.Y. Life Ins. Co. v. Fulton Dev. Corp., 271 N. Y. Suppl. 563 (N.Y.).
Fisher v Norman Apt., Inc., 72 Pac. (2d) 1092 (Cal.).
Andrew v. Home Savings Bank, supra.
Alter v. Clark, supra.
Wilcox v. Goess, 92 Fed. (2d) 8 (2nd Cir.).

9. When the owner is adjudicated a bankrupt, the legal title to the real property passes to the trustee in bankruptcy who becomes the owner thereof, including the right to the rents to the same extent as a grantee if the mortgagee has not entered possession or procured the appointment of a receiver prior to bankruptcy.

Bankruptcy Act, Sec. 70a (11 U.S.C.A. 110a).
Annotation—A.L.R., Vol. 75, p. 1526.
Alter v. Clark, 193 Fed. 153.
Isaacs v. Hobbs, 282 U.S. 734.
Bindseil v. Liberty Tr. Co., 248 Fed. 112 (3rd Cir.).

10. The Bankruptcy Act also puts the trustee in the position of a creditor holding a lien by attachment and cuts off the right of creditors to perfect liens after the bankruptcy petition is filed, which, for want of record or "for other reasons" were not valid at the time of filing the petition. The Bankruptcy Court has no power to perfect a lien by sequestration order or in any other manner which has not become perfected prior to the filing of the petition.

Bankruptcy Act, Sec. 47a (2), (11 U.S.C.A. 75a (2)).
Bankruptcy Act, Sec. 67a (11 U.S.C.A. 107a).
Re: Van Rooy, 21 Fed. Suppl. 431 (Dist. Ct. Ohio).
Re: West—128 Fed. 205 (D.C. Ore.).
Goldman Beckman & Co. v. Smith, supra.
Bindseil v. Liberty Tr. Co., supra.
McCrory Stores Corp., supra.
Re: Foster, supra.
Alexander v. Smithe Mach. Co., supra.
Annotation—75 A.L.R. 1526.
Meier & Frank Co. v. Sabin, 214 Fed. 231 (9th Cir.).

11. Appellants' petitions (now under consideration), seeking the rents in the possession of the trustee, are equivalent to actions against the owner for the recovery of rents collected by him prior to foreclosure and sale, and it is well settled that an owner

in possession cannot be sued for rents by a mortgagee out of possession. The mere fact that the claims are being asserted in the Bankruptcy Court does not change the legal effect of the proceeding.

Teal v. Walker, 111 U.S. 242.
Jones on Mortgages, Sec. 827 (8th ed.).

12. The order requiring the trustee to keep separate accounts did not and could not constitute in law a sequestration of the rents for the benefit of the mortgagee because

(a) the order was merely for the maintenance of separate accounts as to all properties, encumbered or unencumbered; the appellants are not designated therein by name or otherwise, nor is there any language indicating that it was made for their particular benefit.

Opinion by Judge Fee—Record, pp. 131-133.

(b) Sequestration could not be made, in any event, after the filing of the petition in bankruptcy because it would constitute the perfection of a lien in violation of Sec. 47a (2) and Sec. 67a of the Bankruptcy Act.

Bankruptcy Act, Sec. 47a (2) (11 U.S.C.A. 75a (2)).
Bankruptcy Act, Sec. 67a (11 U.S.C.A. 107a.)
Re: Foster, supra.
Alexander v. Smithe Mach. Co., supra.
Re: Pine Tree Lumber Co., supra.
Bindseil v. Liberty Tr. Co., supra.

(c) Sequestration is a provisional remedy, and the Bankruptcy Court has no jurisdiction to grant a provisional remedy in aid of a main proceeding pending in another tribunal.

Opinion of Judge Fee—Record, pp. 127, 129, 130, 133, 134.
1 C. J. 945.
Pomeroy's Equity Juris., Vol. 5, p. 3.

(d) There can be no sequestration of future rents. Only property or funds in actual existence may be sequestered.

Hagemann v. Pinska, 37 S.W. (2d) 463.
57 C. J. 174.
John Miller Co. v. Harvey Merc. Co., 165 N.W. 558.

13. Mortgagees cannot, in any event, assert a claim to rents until establishment of actual deficiency, and deficency judgments entered after bankruptcy has intervened are not conclusive on trustee where mortgagee is purchaser at foreclosure sale. Trustee has the right to show that the value of the property is sufficient to satisfy the mortgage debt.

Re: Cigar Stores Realty Holdings, Inc., 69 Fed. (2d) 823 (2nd Cir.).
Re: Benevolent & P. Order of Elks, 9 Fed. Supp. 883 (D.C.N.Y.).
Re: Paramount Publix Corp., 85 Fed. (2d) 42 (2nd Cir.).
Annotation—105 A.L.R. 600, 106 A.L.R. 1121.
Re: Soltmann, 238 Fed. 241.
Re: McAusland, 235 Fed. 173, 179 (D.C.N.J.).
Re: Davis, 174 Fed. 556 (3rd Cir.).
Re: Dix, 176 Fed. 582 (D.C. Pa.).
Re: Barrett & Co., 27 Fed. (2d) 159 (D.C. Ga.).
Re: Brady Foundry Co., 3 Fed. (2d) 437 (7th Cir.).

ARGUMENT

The Court below predicated its decision on the basic proposition that under the Oregon law which must be applied, a mortgagor retains title to the real property, together with the right of possession and the right to collect and appropriate the rents to his own use; that a pledge of **future rents** does not create a lien until after default and then only when the mortgagee obtains peaceful possession or commences a foreclosure proceeding and obtains the appointment of a receiver therein who collects the rents. The lien will then attach to such rents. There can be no substitute for this method of acquiring a lien; that appellants did not acquire such a lien prior to commencement of the bankruptcy proceeding; that the trustee in bankruptcy acquired all of the title of the owner, the right to and the actual possession, and the owner's right to collect, retain and appropriate the rents, with the added protection of Sec. 47a (2) which placed him in the position of a creditor holding a lien by attachment, and of Sec. 67a which cut off the right to perfect liens after the filing of the bankruptcy petition, and that no sequestration of the rents was made in this case in the bankruptcy proceeding for the benefit of the mortgagees, nor could such sequestration be made because

(a) it would be equivalent to creating a lien in favor of the mortgagees in violation of the aforesaid provisions of the Bankruptcy Act; and

(b) sequestration being a provisional remedy, the Bankruptcy Court would be without jurisdiction to grant the same in aid of foreclosure proceedings prosecuted in other tribunals.

The opinion of Judge Fee is printed in full (R. 124 to 134).

It is a concise yet comprehensive discussion of every phase of the law applicable to the case at bar. His conclusions are fully supported by the authorities he quotes and by the additional authorities referred to herein.

Appellants' attack upon this decision is due to the

(1) failure to recognize that in Oregon, as in most jurisdictions, a pledge of future rents does not, ipso facto, create a lien but can be ripened into a lien only by obtaining peaceful possession of the mortgaged property or by the appointment of a receiver in foreclosure proceedings, and the collection of rents by such receiver;

(2) failure to recognize that a mortgage on real property pledging rents and profits has, in reality, two phases:

(a) a lien upon the real property which is effective at once, and

(b) a **contract for a lien** on future rents which can ripen into a lien only in the manner referred to above. It is similar to a chattel mortgage on future crops or on after acquired property;

(3) failure to have in mind that upon the filing of a petition in bankruptcy (if adjudication follows thereafter) the title to the property vests in the trustee as of the commencement of the proceeding, with all the incidents of ownership; that the Bankruptcy Act clothes the trustee as such owner with the additional protection of a creditor holding a lien by attachment, and that the right to perfect liens after the filing of the petition is cut off. Hence, a mortgagee (in states like Oregon) is prevented from acquiring any lien upon the future rents after the filing of the petition in bankruptcy if he has not perfected such a lien prior thereto in the manner recognized as sufficient by the Oregon law;

(4) failure to recognize the distinction between the estate acquired by a trustee in bankruptcy (who has all of the rights referred to above) and a receiver appointed in an equity receivership who is merely a custodian.

OREGON LAW

The law in Oregon is crystallized in Sec. 5-112 Oregon Code and in the following decisions.

Section 5-112, Oregon Code, provided:

> "Mortgage not a conveyance—Foreclosure—Possession — Receivers. — A mortgage of real property shall not be deemed a conveyance so as to enable the owner of the mortgage to recover possession of the real property without a foreclosure and sale according to law;"

The following portion was added by the 1927 amendment:

> ". . . . provided, that nothing in this act contained shall be construed as any limitation upon the right of the owner of real property to mortgage or pledge the rents and profits thereof, nor as prohibiting the mortgagee or pledgee of such rents and profits, or any trustee under a mortgage or trust deed from entering into possession of any real property, other than farm lands or the homestead of the mortgagor or his successor in interest, for the purpose of operating the same and collecting the rents and profits thereof for application in accordance with the provisions of the mortgage or trust deed or other instrument creating the lien, nor as any limitation upon the power of a court of equity to appoint a receiver to take charge of such real property and collect such rents and profits thereof."

This statute was construed and its meaning and effect established in a great many cases, among them the following:

Teal v. Walker, 111 U.S. 242.
Thomson v. Shirley, 69 Fed. 484 (D.C. Or.); aff'd Couper v. Shirley, 75 Fed. 168 (9th Cir.).
Savings & Loan Soc. v. Multnomah County, 169 U.S. 421.
State ex rel. Nayberger v. McDonald, 128 Or. 684, 695, 696—274 Pac. 1104 (Decided after amendment).
McKinney v. Nayberger, 138 Or. 203-215—2 Pac. (2d) 1111—6 Pac. (2) 228-229 (Decided after amendment).
Schleef v. Purdy, 107 Or. 71-76.

The applicable quotations from these decisions will be found at Pages 1 to 5 of the appendix.

These cases establish that in Oregon the mortgagee is not entitled to the rents "until he takes possession" by foreclosure and sale; that prior to 1927 possession could not be had prior to sale, by Receiver or otherwise even though there was a stipulation therefor in the mortgage because such stipulations were deemed against public policy.

The amendment now permits a stipulation pledging rents and the taking of possession prior to sale but this can be accomplished only by voluntary surrender or the appointment of a receiver in foreclosure proceedings as provided by the statute. There is in Oregon no substitute for this method of obtaining possession.

THE PLEDGE OF RENTS DOES NOT CREATE A LIEN. IT IS MERELY A CONTRACT FOR A LIEN. IT DOES NOT BECOME A LIEN UNTIL ACTUAL POSSESSION IS TAKEN EITHER THROUGH VOLUNTARY SURRENDER OR THROUGH A RECEIVER APPOINTED IN A FORECLOSURE PROCEEDING. THE LIEN ATTACHES ONLY TO THE RENTS COLLECTED BY SUCH RECEIVER.

Wiltsie on Mortgage Foreclosure, 4th Ed., Vol. 1, Sec. 556, says:

"Sec. 556 . . . . . **until the mortgagee takes possession of the premises or files a bill for foreclosure and procures the appointment of a receiver, the mortgagor is 'owner to all the world', and is entitled to all the profits made.**

A mortgage may contain a specific provision assigning the rents and profits of the mortgaged premises as well as the land itself as security for the indebtedness. Such a provision does not ordinarily entitle the holder of the mortgage to specific rents and profits while the property is in possession of the mortgagor or persons **claiming under him** even though there has been a default. A provision pledging rents and profits, after default, merely entitles the mortgagee to recover such rents and profits **by taking possession or by means of a receiver.** Where a mortgage assigns rents and profits, upon a default, as a further security, the holder of a senior mortgage, after a default, is **not entitled to the rents and profits collected by a receiver appointed in a foreclosure suit brought by a junior mortgagee."**

In **Grether v. Nick, 55 A.L.R. 525-532 (Wis.)**, the Court said:

"All of the authorities agree that a pledge of rents and profits **does not create any lien** upon the rents and profits until the mortgagee acquires possession, and that all rents and profits paid to the mortgagor prior to taking possession by, or the appointment of, a receiver belong to the mortgagor. All authorities agree that a pledge of rents and profits vests in the mortgagee a right thereto which equity will recognize and enforce in a proper manner. As already stated, **the only way** in which it can be enforced in this state **is by the appointment of a**

receiver under circumstances justifying such procedure."

A clause pledging the rents is only "an inchoate right" (**A. B. C. Elev. Co. v. Bond & Mtg. Guar. Corp., 278 N.Y. Suppl. 880**):

> "Though the rents were pledged . . . . title to such rents, as they became due and were collected, remained in the owner of record until the pledge was made effective, and the owner of the equity divested of title to the rents by appointment of a receiver or by assignment." (Women's Hospital v. 67th St. Realty Co., 95 A.L.R. 1031-1034 (N.Y.).)

In **Kooistra v. Gibford, 207 N.W. 399 (Iowa)**, the Court said:

> "The law is well settled in this state that a mortgagee **has no lien** upon the rents and profits arising from the mortgaged premises under a clause merely pledging the same as security for the debt, and **without making the same a present lien thereon** until an action to foreclose the mortgage is commenced and the appointment of a receiver requested." (Citing many cases.)

Such a provision in a mortgage

> "does not operate as a present lien." (**Hakes v. North, 203 N.W. 238 (Iowa)**.)

Such a provision

> "did not create a lien on the rents. . . . It only conferred a right upon the mortgagee to impose a lien." (**Burgess v. Lasby, 9 Pac. (2d) 164-167 (Mont.)**.)

It creates only "a potential lien" and

> "limited the perfection of his inchoate right to

> the time when he shall invoke the aid of a court of equity . . . and must be perfected . . . by asserting the right by some definite action looking toward possession and subjection. . . . . Until that is done, he does not acquire a vested lien that will prevent a complete lien imposed subsequent to his inchoate lien. from becoming prior and paramount in effect." **(Southern Tr. Co. v. First City Bank, 82 S.W. (2d) 205.)**

Such a provision "operates only as contracts for a lien" **(Norwood Sav .Bank v. Romer, 183 N.E. 45 (Ohio).)**

> In 4 **A.L.R. 1410**, annotation, the author says:
>
> "The **great weight of authority** as regards all of these various forms of pledges is to the effect that the mortgagee **does not** thereby **acquire a lien on the rents** and profits, which prevents a subsequent lien from acquiring priority in the absence of some action on his part to reduce the rents and profits to his possession."

Giving effect to the rule that a pledge of rents does not create a present lien, the courts have given priority to lien claimants who have first obtained possession of the rents. Thus junior mortgagees were held entitled to the rents as against senior mortgagees. (Sullivan v. Rosson, 4 A.L.R. 1400 (N.Y.); Lincoln Sav. Bank v. Realty Assoc., 67 Fed. (2d) 895 (2nd Cir); First Joint Stock Land Bank v. Armstrong, 262 N.W. 815.)

Creditors who have attached rents were given priority over antecedent mortgagees. (Fisher v. Norman Apartments, 72 Pac. (2d) 1092.)

Chattel mortgagees holding crop mortgages were given priority over mortgagees claiming a lien upon the land as well as crops. (Bank of America v. Bank, 28 Pac. (2d) 86 (Cal).)

APPELLANTS' RIGHT TO PERFECT LIENS UPON FUTURE RENTS WAS CUT OFF BY THE INTERVENTION OF BANKRUPTCY.

When the bankruptcy petition was filed none of the appellants were in possession of the mortgaged premises; none of them (except Portland Trust and Savings Bank) had commenced any foreclosure proceedings, and none of them had obtained the appointment of a receiver.

Section 47 (a) (2), (11 U.S.C.A., Sec. 75), provides:

> "And such trustees, as to all property in the custody, or coming into the custody, of the bankruptcy court shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon. . . ."

Section 67 (a) (11 U.S.C.A., Sec. 107), provides:

> "Claims which for want of record **or for other reasons** would not have been valid liens as against the claims of the creditors of the bankrupt shall not be liens against his estate."

In **Isaacs v. Hobbs, 282 U.S. 734-737,** the Court held:

> "Upon adjudication, title to the bankrupt's property vests in the trustee with actual or construc-

> tive possession, and is placed in the custody of the bankruptcy court. Mueller v. Nugent, 184 U.S. 114, the title and right to possession of all property owned and possessed by the bankrupt **vests** in the trustee **as of the date of the filing of the petition in bankruptcy. . . . .**"

The following authorities, construing the aforesaid provisions of the bankruptcy act, support the proposition that after filing of a petition in bankruptcy, liens cannot thereafter be perfected.

In **Fairbanks Steam Shovel Co. v. Wills, 240 U.S. 642-649,** the Court held:

> "Appellant's title was **not perfected, as against the trustee in bankruptcy,** by taking possession of the dredge under the mortgage after the filing of the petition in bankruptcy, and before the adjudication. Since the amendment of Sec. 47a-2 of the Bankruptcy Act by the act of June 25, 1910, trustees have the rights and remedies of a lien creditor or a judgment creditor as against an unrecorded transfer."

In **Meier & Frank Co. v. Sabin, 214 Fed. 231-233 (9th Cir.),** the Court held:

> Under this provision of the statute (referring to 47a (2), Bankruptcy Act) . . . . An **agreement,** therefore, which prior to this amendment would have been valid between the parties, **may not be valid** as **against the trustee."**

In **re Van Rooy, 21 Fed. Supp. 431-432 (D.C. Ohio),** the trustee collected rents from the mortgaged premises. After the sale of the property, the mortgagee petitioned the bankruptcy court "for an

order to segregate the aforesaid rents thus collected". The mortgagee took no other action "to assert its claim to the rents as distinguished from its lien on the real estate". The mortgage contained a provision giving the mortgagee, upon default, the right of possession and to have a receiver appointed and to collect the rents and profits. The Court held:

> "This particular question is rather controlled by the provision of section 47a of the act, as amended, 11 U.S.C.A. 75(a).
>
> . . . . . .
>
> (1) True, when the petition was filed and the trustee took possession, the rents did not come into his custody, but accrued later, and therefore should properly be regarded as funds 'coming into the custody of the bankruptcy court'. **When they reached such custody, they were immediately impressed with the foregoing lien** (of attaching creditors).
>
> (2, 3) Funds so collected by a trustee are subject to valid prior liens. Vincent v. Tafeen, 1 Cir., 40 F. (2d) 823. But, as noted above, in this case the prior lien of the mortgagee had **not been made effective in the manner provided in the mortgage and was only inchoate.** If the mortgagee desired to make this lien effective, it should have brought foreclosure proceedings with the court's consent, or, without doing this, obtained from this court the appointment of a receiver to collect these rents for its benefit or at least it should have made some such attempt. Its **mere motion for an order requiring the trustee to segregate** or set apart the rentals **was not sufficient."** (Cases.)
>
> (Matter in parenthesis inserted.)

This rule was applied in the following additional cases, to-wit:

Re: Foster, 9 Fed. Cas., p. 523, Case No. 4963, aff'd. 9 Fed. Cas., p. 572, Case No. 4982.
Alexander v. Smithe Machine Co., 143 N.E. 321—2 A.B.R. (N.S.) 500 (Mass.).
Goldman Beckman & Co. v. Smith, 2 A.B.R. 104-107.
Re: Bindseil v. Liberty Trust Co., 248 Fed. 112 (3rd Cir.).
Industrial Finance Corp. v. Cappelmann, 284 Fed. 8 (4th Cir.).

Under these authorities the appellants (mortgagees) were clearly precluded from perfecting a lien upon the future rents, after the filing of the bankruptcy petition, in any manner whatsoever, whether by a receiver in a state court, sequestration, or taking of possession. Any attempt to perfect a lien would be a violation of Secs. 47 and 67 of the Act.

THE ORDER CONTAINING PROVISION TO KEEP SEPARATE ACCOUNTS DID NOT AND COULD NOT CONSTITUTE IN LAW A SEQUESTRATION OF THE RENTS FOR THE BENEFIT OF THE MORTGAGEES.

The order which appellees claim to be a sequestration is as follows:

"ORDERED that said trustee will **keep separate accounts** of all moneys coming into his possession from each **of the several properties of the debtor** or its said affiliate, and that the trustee's accounts shall be kept so that all income

and revenues received and expense incurred in the operation of each of such properties can at all times be ascertained and segregated."

Appellants frequently repeat two serious erroneous assertions in discussing the effect of this order. **First,** they say that the order directs the segregation of "all moneys". The order does not direct the manner in which any funds were to be maintained. It gives directions as to **accounting or bookkeeping** merely. **Second,** they erroneously say that the order directed the keeping of separate accounts as to the properties covered by **appellants' mortgages,** leaving the implication that the order was made for their special benefit. The order directs the maintenance of separate accounts as to **all** properties of the bankrupt, **whether encumbered or unencumbered.** There is not the least intimation that the accounts were to be kept only as to the mortgaged properties or that the accounts were to be kept only as to properties covered by appellants' mortgages.

At the time the said order was made, the mortgagees had not, by petition or otherwise, requested any sequestration of rents. The mortgagees had **refused to submit themselves to the jurisdiction of the Court, and appeared specially.**

The Court did not adopt the recommendation of the Master that "in particular that separate accounts be kept of the moneys received from the operation of each of the properties covered by said mortgage". (Word "said" erroneously used. Should read "covered by a separate mortgage.)

When Eakin was appointed trustee in place of Twining, the order contained the same provision as quoted above.

Appellants now contend that this order was a sequestration for their benefit.

Judge Fee held (R., 131-133):

> "The Court did direct therein that the accounts of each parcel be kept separate but did not express any intention of giving any mortgagee an interest therein. It was only sound bookkeeping. Under these circumstances the mortgagees, having taken no steps to protect their supposed rights, could not prevail even under the decisions above cited.
>
> . . . . . .
>
> The Bankruptcy Court should not be required to sequester rents in the hands of its trustee for the benefit of adverse parties sueing the trustee in alien tribunals."

There is no foundation whatsoever for the appellants' contention that this order was a sequestration for their benefit. The very fact that the Court rejected the Master's recommendation which made some reference to mortgagees (generally—not these appellants) and merely provided for the keeping of separate accounts generally as to all properties—encumbered or unencumbered — demonstrates conclusively that the Court, in making that order, sought to avoid the very consequence which appellants now attach to the order.

Appellants did not treat this order as a sequestration for their benefit because the very petitions

which the Court now has under consideration, filed long after the said order was made, pray that the rents be set apart for them (see prayer of petitioners, R. 25, 33, 52).

The order as made **does not refer to the mortgagees.** It contains no intimation that it was made for the benefit of the mortgagees. It does not require that the **"moneys"** should be "segregated" or set apart for the mortgagees, or that it should be held for the mortgagees. The order was not limited to the properties covered by appellants' mortgages nor to mortgaged properties at all. It required separate accounts to be kept of **all** of the many properties owned by the bankrupt, **whether encumbered or not.**

The order does not deal with moneys at all. **It deals only with the subject of accounting or bookkeeping.** It contemplates that the moneys collected should be and remain a single general fund. It is the bookkeeping system only that is dealt with.

We cannot presume that the Court intended to make a void order. To construe the order as appellants contend for would render it void because

(a) It would be equivalent to perfecting a lien on the rents after bankrupty in violation of the Bankruptcy Act;

(b) it would be equivalent to granting a provisional remedy in aid of proceedings pending or to be prosecuted in other courts;

(c) there could be no substitute for the method

provided by the Oregon law for obtaining a lien on rents which contemplates actual possession by the mortgagee or a receiver;

(d) sequestration can only be made of property or funds in existence and not on future rents.

Provisional remedies can only be granted in, and in aid of, a proceeding pending in the court allowing the provisional remedy. We are not aware of any instance in which a provisional remedy was granted in aid of proceedings pending in other courts or as independent relief.

In **1 Corpus Juris, 945,** the rule is stated as follows:

> "A provisional remedy is a collateral proceeding, permitted only in connection with a regular action, and as one of its incidents; one which is provided for present need, or for the occasion, that is, one adapted to meet a particular exigency."

THE FEDERAL COURT DECISIONS IN BANKRUPTCY CASES CLEARLY SUPPORT APPELLEES' POSITION.

The following decisions were rendered in bankruptcy proceedings and involved mortgages in states where the law governing the relation between the mortgagor and mortgagee is the same as it is in Oregon:

In re: Hotel St. James Co., 65 Fed. (2d) 82-84 (9th Cir.), the mortgage contained a provision authoriz-

ing the mortgagee to enter and take possession, to collect the rents and for the appointment of a receiver. The mortgagee did not take possession or have a receiver appointed prior to bankruptcy. The question as to the ownership of rents arose in the same manner as in the case at bar, to-wit: by petition to the bankruptcy court for an order requiring the trustee to turn over the rents. The Court sustained the trustee's right to the rents.

In **Dallas Trust & Savings Bank v. Ledbetter, 36 Fed. (2d) 221-222 (5th Cir.)**, the mortgage contained a provision pledging the rents and profits. **Foreclosure proceedings were commenced prior to bankruptcy but no receiver was appointed.** Prior to the date set for the sale, the owner was adjudged a bankrupt. The trustee thereafter collected rents, and the mortgagee later made application to the Bankruptcy Court therefor. The Court held:

> "The general rules, that a mortgage is but security for a debt, that, until it is foreclosed, the title and possession remain in the mortgagor, and that the mortgagor is not liable for rent while he remains in possession, **prevail in Texas.** Willis v. Moore, 59 Tex. 628. . . .
>
> . . . . . .
>
> It hardly need to be said that the trustee in bankruptcy succeeded to the rights of the bankrupt. There had been no foreclosure sale on the 1st of April, when under any view the rent became due and payable."

Appellants attempt to distinguish this case by pointing out that the "mortgagee did not apply to

the bankruptcy court until after the rents accrued." This was not the basis of the court's decision. It was decided squarely upon the law of Texas which adheres to the doctrine that a mortgage does not entitle the mortgagee to rents and profits.

It is urged that the later decision of the Court of Appeals of the Fifth Circuit in **Florida Bank vs. U. S., 87 Fed. (2d) 896,** adopted a different principle. That is not the case. In the **Dallas case** the Court had under consideration a **Texas mortgage,** which does not pass any title to the mortgagee, whereas in the **Florida Bank case** the Court had under consideration a **Florida deed of trust,** and in that State a deed of trust is distinguished from a mortgage and is held to pass the legal title to the grantee and with it the right of possession (**Soutter v. Miller, 15 Fla. 625**).

Appellants' counsel overlook the proposition that the various Courts of Appeal are not dealing with problems of federal law. They deal in each case with the law of the state in which the transaction takes place, and consequently, in one Circuit there may be, and indeed there are, cases in which the law of states embraced in that Circuit differs materially.

Appellants' counsel do not fairly present the facts in the **Florida Bank case.** In view of the distinction that is made in Florida between a mortgage and a trust deed, it was misleading to state that the transaction was a mortgage. In that case

the **grantee under the trust deed was actually in possession** of the property at the time that the re-organization proceedings were initiated. In the Florida case **the re-organization proceedings were dismissed. They did not,** as in the case at bar, **enter an order of liquidation.** That is very important. The dismissal of the re-organization proceedings left the situation as though no proceeding were ever initiated, whereas the entry of an order of liquidation is an order of adjudication as of the date of the initiation of the bankruptcy proceeding.

In re: McCrory Stores Corp., 73 Fed. (2d) 270-271 (2nd Cir.), the Court held:

> "But the appellants cannot prevail for an additional reason. Before the lessors filed their petition herein or had otherwise asserted any claim to the accrued sub-rents, a petition in bankruptcy had been filed by McCrory Stores Corporation, an adjudication entered and a trustee elected. The latter stood in the position of a judgment creditor armed with an execution.
>
> Under the decisions of the New York state courts and of the federal courts, when applying the New York law, it is well settled that **an assignee of future rents** who has done nothing to perfect his rights **will not prevail over** an execution creditor or **trustee in bankruptcy.** Sullivan v. Rosson, 223 N.Y. 217, 119 N.E. 405, 4 A. L.R. 1400; In re: Brose (C.C.A.) 254 F. 664; In re: Berdick (D.C.) 56 F. (2d) 288.
>
> . . . . . .
>
> **But an agreement to create a lien is quite different from such an interest as a vendor's lien, a resulting trust, or other vested equitable title.**

Shear Co. v. Currie (C.C.A.), 295 F. 841; In re: Rosenberg (D.C.), 4 F. (2d) 581; First State Bank of Amarillo v. Jones, 107 Tex. 623, 183 S. W. 874."

The same rule was applied in the following additional Federal cases:

Re: Brose, 254 Fed. 664 (2d Cir.).
Re: Humeston, 83 Fed. (2d) 182 (2nd Cir.).
Willcox v. Goess, 92 Fed. (2d) 8-12 (2nd Cir.).
Alter v. Clark, 192 Fed. 153-157 (D.C. Neb.).
Smith v. Schulte, 91 Fed. (2d) 732 (2nd Cir.).
Bindseil v. Liberty Trust Co., 248 Fed. 112 (3rd Cir.).
75 A.L.R. 1526, ann.
Re: Israelson, 230 Fed. 1000 (D.C. N.Y.).

Quotations from these cases will be found at pages 15 to 20 of the Appendix.

DISCUSSION OF APPELLANTS' AUTHORITIES

American Trust Company v. England, 84 Fed. (2d) 352 (9th Cir.), is cited as authority for the proposition that the mortgagee is entitled to the rents from the time he makes demand therefor upon the Trustee in Bankruptcy. That case does not support this proposition. The question was not presented or passed upon by the Court and was not the basis of its decision.

The case did not involve rents in the possession of a trustee in bankruptcy **of the owner.** The rents had been collected and were in the possession of the trustee in bankruptcy **of a third mortgagee** who ob-

tained peaceful possession with the "implied consent" (as the Court found) of the owner. The first mortgagee petitioned the Court for an order sequestering these rents for its benefit. Such an order was made without objection from the third mortgagee or the owner. Thereafter the property was surrendered to the first mortgagee who petitioned "for the release of the impounded funds". The owner intervened and, for the first time, asserted a claim to the rents in the possession of the third mortgagee.

Under these circumstances, the Court said:

> "The demand of the appellant upon the trustee (of the third mortgagee) for the sequestration of rents, and the **Referee's order for the sequestration,** is the equivalent of the taking of possession by the appellant (first mortgagee) under its trust instrument." (Matter in parentheses inserted.)

In other words, the owner was asserting a claim to rents collected by a mortgagee in possession, and it is, of course, well settled that an owner cannot assert a claim for rents as against a mortgagee in possession until he has paid the mortgage debt.

There is nothing in the decision to indicate that the Court would have made the same ruling **if the owner, or the trustee in bankruptcy of the owner, had been in possession and had collected the rents.**

Under Sullivan v. Rosson, supra, and Lincoln Savings Bank v. Realty Associates, supra, the Court would have awarded the rents to the trustee of the third mortgagee if it had asserted a claim thereto

as against the first mortgagee. The owner could only support his claim to the rents on the strength of his own title and not by the weakness of his adversary, and since the owner was out of possession and an actual sequestration of the rents had been made in favor of the first mortgagee, without objection from the owner or the third mortgagee, the Court properly awarded the rents to the first mortgagee.

In the case at bar, the trustee of the owner was in possession of the property and of the rents, and hence is in a position to assert a superior right thereto as against the mortgagees.

The case of **Duparquet v. Evans, 297 U.S. 216,** merely held that the appointment of a receiver in a foreclosure proceeding does not constitute an act of bankruptcy. The Court pointed out that the receivership referred to in 77-B was the kind that was generally known as an equity receivership.

When the Court said that "bankruptcy will not override a valid mortgage lien", it referred to a lien **created and perfected prior to the filing of the bankruptcy petition.** It did not hold that **contracts for a lien** could be perfected subsequent to the filing of a petition in bankruptcy.

When the court spoke of sequestration, it referred to **sequestration,** which would be a **provisional remedy in the foreclosure proceeding** and be, in legal contemplation, as unequivocal as actual possession by the mortgagee.

Sequestration contemplates rents in existence, and an effective impounding of such fund for the benefit of the mortgagee. It seems to us there is no such thing as sequestering moneys **not in existence** and which may never come into existence.

In the case of **Straton v. New, 283 U.S. 318,** in answer to a specific certified question, the Court held only that bankruptcy will not invalidate **existing liens.** The Court was careful to point out that when a bankruptcy petition is filed

"liens cannot thereafter be obtained".

In the case at bar the mortgagees had no liens **on the future rents** at the time the bankruptcy petition was filed. They had only agreements for liens to become effective when the rents accrue and then only (in the State of Oregon) by taking possession and collecting the rents or by the appointment of a receiver in foreclosure proceedings.

In **Continental Bank & Trust Company vs. Nineteenth and Walnut Streets Corp., 79 Fed. (2d) 284,** cited by the appellant, the Court dealt with a **Pennsylvania** mortgage which conveys to the mortgagee the legal title and right of possession (Appendix, p. 4). The **mortgagee** was **in actual possession** of the property **prior to** the **commencement of the reorganization proceeding,** not only by virtue of the law which gave it the right to possession, but also **by virtue of a written consent.** The Court said:

> "Under the laws of Pennsylvania, the owner of a defaulted mortgage, ...

> is entitled to take possession of the mortgaged premises and collect the rents and profits accruing thereon. . . . . .
>
> Moreover, in addition to the warrant of such authorities, Continental (mortgagee) had the written authorization of the mortgagor. . . ."

The cases referred to by that court (same as relied on by appellants), were decided in jurisdictions where the mortgage passes the legal title to the mortgagee and carries with it the right to possession and rents.

Re: **Shelburne, Inc., 91 Fed. (2d) 190.** The Court dealt with a **New Jersey** mortgage. In that jurisdiction the mortgage passes the legal title to the mortgagee (Appendix, p. 3). In that case foreclosure proceedings were commenced and a receiver appointed who **took and retained possession two years prior to the commencement of the reorganization proceeding.**

In re: Wakey, 50 Fed. (2d) 869 (7th Cir.), involved an **Illinois** mortgage which passes title to the mortgagee and makes him "virtual owner". (Appendix, p. 2).

This Court has rejected and refused to follow that case (Hotel St. James case), due, no doubt, to the erroneous assumption which the Court of Appeals of the 7th Circuit indulged in when it said:

> "Assuming as we do that the trustee in bankruptcy occupies the same position as a receiver appointed in a suit in equity, where no directions

> appear as to the disposition of the rents and profits, there seems no escape from the conclusion that payments out of such funds should be made to the lien holders in the order of their priority."

A trustee in bankruptcy does not occupy the same position as a receiver in an equity suit. The receiver is merely a custodian; he acquires no title of any character, whereas the trustee in bankruptcy becomes not only the owner of the title but has the added superior right of a creditor holding a lien by attachment.

Even that court recognized the principle that **the mortgage does not create a lien upon future rents.**

In re: Industrial Cold Storage & Ice Co., 163 Fed. 390, the question passed upon by the Court is not involved in the case at bar. It is the same question which was specifically reserved by the Court below in this case and is excluded from consideration on this appeal. It involved an application to have the rents **applied to the payment of taxes, etc.,** and not an application to turn the rents over to the mortgagees.

The court was dealing with a **Pennsylvania mortgage** and for that reason held:

> "That a lien creditor under conditions similar to those now presented is in equity the real owner of the land, and is therefore entitled to have its rents, issues and profits applied to the discharge of his lien."

This is not true in Oregon.

Prudential Ins. Co. v. Liberdar Holding Co., 74 Fed. (2d) 50, 51, 52 (2nd Cir.), is cited for the proposition that the mortgagees are entitled to the rents merely by making application therefor to the Bankruptcy Court. That case was an **equity receivership** and not a bankruptcy case. The equity receiver had no title or interest superior to that of the mortgagees for he was a custodian merely. Hence the mortgagee could perfect and assert his lien upon the rents at any time. That is not true as against a trustee in bankruptcy. The Court in that case clearly recognized the superior right of the trustee in bankruptcy. Said the Court:

> "We recently said in Matter of McGrory Stores Corporation, 73 F. (2d) 270, that 'an assignee of future rents (who has done nothing to perfect his rights) **will not prevail over an execution creditor or trustee in bankruptcy.** Sullivan v. Rosson, 223 N.Y. 217, 119 N.E. 405, 4 A.L.R. 1400; In re: Brose (C.C.A.), 254 F. 664; In re: Berdick (D.C.), 56 F. (2d) 288'. We think this is true of any assignment of future rents that is less than a transfer to the assignee of outright ownership rather than of the rights of a mere security holder (cases). In the case at bar **nothing was done by the creditor to appropriate** or even to make claim to any interest in the **rents until it filed its petition on December 15, 1933.**"

The court denied the mortgagees the rents collected by the equity receiver between the time of appointment and the time that the mortgagees made application, but allowd the rents thereafter because the equity receivership did not like the Bankruptcy

Act cut off the right to perfect a lien.

In the case of **Petition of Cox, 15 Fed. (2d) 764,** the decision of the District Court as well as of the Circuit Court of Appeals was predicated solely on the "applicable local law" of **Massachusetts** (p. 2 Appendix).

The trustee in bankruptcy never took or asserted any claim to possession. The controversy was over rents collected by the mortgagee in possession.

Appellants misconstrue the language employed by the author of the Annotation in 75 A.L.R. 1526. They seize upon the use of the phrase "up to the time the mortgagee takes action" and conclude that any application to the Bankruptcy Court for the rents would suffice.

"Takes action" means "brings a bill to foreclose or enter". (See full sentence from which phrase was culled.)

The element common to all the cases cited by appellants is that in all of the states in which the mortgages were made, the mortgagee, by virtue of the mortgage and the law of the state applicable thereto, had the legal title, the immediate right of possession, and the immediate right to the rents. The **mortgagor merely has a right of redemption.** Hence, when bankruptcy ensues, the only thing that passes to the trustee in bankruptcy in those cases is the equity of redemption and not the legal title or the incidental right to the rents from the mortgaged

property. Whereas, in states like Oregon, New York, Texas, and others, the legal title and the incidental right to the rents and possession remains with the mortgagor, and which passes to the trustee in bankruptcy. He becomes the owner thereof to the same extent as a grantee under a deed, with the added right conferred upon him by Sections 47a and 67a, etc., of the Bankruptcy Act which gives him the rights of a creditor holding a lien by attachment and the right to cut off the perfection of any liens which "for other reason" were inoperative at the time of bankruptcy.

MORTGAGEES ARE NOT IN ANY EVENT ENTITLED TO RENTS UNTIL AFTER THE ASCERTAINMENT OF A DEFICIENCY. A DEFICIENCY JUDGMENT ENTERED AFTER BANKRUPTCY HAS INTERVENED IS NOT CONCLUSIVE WHERE MORTGAGEE IS THE PURCHASER AT FORECLOSURE SALE.

When the Special Master rendered his report, there were no deficiency judgments in existence. The applications for rents are not based upon any ascertained deficiency.

Under these circumstances, the mortgagees are not entitled, in any event, to the rents even assuming, without admitting, that they had valid liens on the rents in question.

In The Matter of Cigar Stores Realty Holdings, Inc., Bankrupt, 69 Fed. (2d) 823, (2nd Cir.), the Court held:

> "In any event, a condition precedent to the right of the mortgagee to rents collected is proof of a deficiency. Associated Co. v. Greenhut, supra; Primeau v. Granfield (C.C., 184 F. 480). There is none here."

It is well settled that a deficiency judgment rendered after bankruptcy has intervened, is not conclusive upon the actual existence of a deficiency **where the mortgagee is the purchaser at the foreclosure sale,** and the Bankruptcy Court may determine the actual value of the mortgaged property for the purpose of determining whether the value is sufficient to satisfy the mortgage indebtedness.

Re: Benevolent & P. Order of Elks, 9 Fed. Suppl. 883 (D.C.N.Y.).
Re: Paramount Publix Corp., 85 Fed. (2d) 42 (2nd Cir.).
Annotation—105 A.L.R. 600, 106 A.L.R. 1121.
Re: Soltmann, 238 Fed. 241.
Re: McAusland, 235 Fed. 173, 179 (D.C.N.J.).
Re: Davis, 174 Fed. 556 (3rd Cir.).
Re: Dix, 176 Fed. 582 (D.C. Pa.).
Re: Barrett & Co., 27 Fed. (2d) 159 (D.C. Ga.).
Re: Brady Foundry Co., 3 Fed. (2d) 437 (7th Cir.).

RESPONSE TO ARGUMENT
PAGES 17 TO 19

Re: Demand for rents or order of segregation.

Appellees do not question the proposition that valid liens perfected prior to bankruptcy are protected by the Bankruptcy Act. We claim only that a pledge of future rents **is not a lien** prior to appointment of a receiver in foreclosure proceedings and that the right to create or perfect liens is cut off by the Bankruptcy Act.

In the case at bar the mortgagees had the right to invoke the jurisdiction of the Bankruptcy Court, and have their mortgage lien enforced.

They could have petitioned

(a) for possession of the property and that the trustee abandon the same; or,

(b) that the Bankruptcy Court determine the value of their securities and ascertain the extent of any deficiency (57 (h) (11 U.S. C.A. 93h);

(c) that the property be sold subject to their liens;

(d) that the property be sold free of lien and to have their liens transferred to the proceeds, with leave to bid the amount of their mortgage liens upon such sale.

By prosecuting foreclosure proceedings in other tribunals, appellants deprived the Bankruptcy Court of jurisdiction to grant them any provisional reme-

dy by sequestration, or otherwise.

Appellants ignore the distinction between the **lien** upon the **real property** and the **contract for a lien on future rents** by virtue of the provisions pledging the rents. The former was valid and entitled to protection in the Bankruptcy Court, but the latter was not because it had not, prior to the filing of the bankruptcy petition, ripened into a lien in the manner required by the Oregon law, and hence, the principles contended for are inapplicable in the case at bar.

RESPONSE TO ARGUMENT PAGES 19 TO 35

Re: Contention that mortgagee is entitled to rents upon taking appropriate action in the Bankruptcy Court.

What constitutes "appropriate action?". . . . . That depends on the legal effect of a pledge of rents according to the local applicable law. In states like Pennsylvania, where the mortgage passes to the mortgagee the title and rents, the trustee takes title subject thereto; he gets only an equity of redemption, and an application to the Bankruptcy Court for the rents may (?) be sufficient. But in states like Oregon, New York, and others where the pledge of rents does not create a lien until the mortgagee has taken possession or procured the appointment of a receiver, then the trustee acquires title

which is not subject to lien on rents, and an application therefor to the Bankruptcy Court would not entitle the mortgagee to the rents and the right to perfect a lien would be cut off.

The cases cited by appellants do not support their contention.

In **Mortgage Loan Co.** case the Court dealt with a **Missouri** mortgage which passed to the mortgagee, title, right of possession and rents (Appendix, p. 3). Immediately upon the appointment of the bankruptcy receiver, the mortgagee demanded that the revenues be segregated for application on the mortgage debt. **The receiver promptly consented to such segregation and application.** Thereafter the court granted the mortgagee leave to continue foreclosure of its mortgage, and **surrendered the possession of the property to the mortgagee.** After the sale and the ascertainment of a deficiency, the mortgagee petitioned for the payment to it of the net rents so segregated.

The property came to the receiver in bankruptcy freighted (under the Missouri law) with a superior right of mortgagee to possession and rents as owner thereof, and was followed by actual sequestration in recognition of the superior right. It was because of the legal status of a mortgagee in Missouri that the Court held:

> "The receiver confessedly took over the bankrupt's property subject to all the then valid existing liens"

which included, of course, the right of possession and rents as owner.

In the case at bar the mortgage did not pass title, right of possession, or rents to the mortgagee, and there was no sequestration prior or after bankruptcy.

In **Re: Hotel St. James Co.,** cited by appellants, this Court sustained the position of the trustee in bankruptcy.

Appellants are in error when they assert (p. 20) that this Court awarded the rents to the trustee in bankrupty "solely for the reason that no application for the rents and profits had been made by the mortgagee until after all the rents had been collected and the property had been sold on foreclosure".

The case was decided on the authority of Re: Brose (New York) because the applicable law of California was the same as in New York. It gave effect to the principle that the owner is entitled to the rents until the pledge of rents ripens into a lien by obtaining the appointment of a receiver.

The reference in that case to the failure to obtain sequestration with the consent of the receiver in possession, as in the Livingston case, was an added reason for the decision.

In commenting on Mortgage Loan Co. v. Livingston, the Court did not say (as appellants assert, p. 21), that the mere application for the rents was the controlling factor, but it was the application for **and**

the actual sequestration to which "the receiver assented", plus the fact that in Missouri the trustee takes title subject to the mortgagee's right to the rents, that was the controlling factor in the Livingston case.

Obviously **this Court did not regard mere application as the equivalent of sequestration.** Had it done so, it would have treated the application in the St. James case as sufficient to warrant awarding the rents to the mortgagee.

The case of **American Trust Company v. England, 84 Fed. (2d) 352,** has already been discussed (p. 34 this brief).

In the **England** and **Livingston** cases, the sequestration had become complete, binding and unassailable by reason of the acquiescence and consent of the owner in each instance, prior to the time when application was made to the Court for the surrender of the rents to the mortgagee. Not so in the case at bar.

In order to make the **England** case analogous to this case it is asserted (pp. 22-23) that the possession by the **trustee of the third mortgagee** is the same as the possession of the rents by a **trustee of the owner.** This ignores the basic rights of an owner in possession. As against him neither first nor third mortgagees acquire any right to the rents prior to foreclosure of sale, except in the manner provided by the Oregon statute. An owner can, if he so chooses, sur-

render possession to any mortgagee.

The owner in that case did not assert any claim at "all stages". On the contrary, the Court found, he did not assert any claim to the rents until after (a) he had with "implied consent" surrendered possession of the property to the third mortgagee, and (b) the rents were, without objection of the third mortgagee, sequestered for the benefit of the first mortgagee.

In support of the contention that mere application to the court will entitle the mortgagee to rents, appellants quote from the England case as follows:

> "The demand of the appellant upon the trustee for the sequestration of rents and **the referee's order for the sequestration,** is the equivalent of the taking of possession by the appellant under its trust instrument. Mortgage Loan Co. v. Livingston."

The making of this order was not opposed by the owner. He could not have opposed it in any event **because he was not in possession,** and had impliedly consented to the third mortgagee's possession. The court did not say that mere application would suffice. It held that the demand for and the unchallenged order of sequestration for the first mortgagee was equivalent to a transfer of possession from the third to the first mortgagee.

There is a difference between an application to turn over rents already sequestered (as in the England and Livingston cases) and an application to

turn over rents not theretofore sequestered (as in the Hotel St. James case and case at bar). In the former case the Court is confronted with an accomplished fact, to-wit: moneys held in trust for the mortgagee for whose benefit it was sequestered. It is no longer concerned with the question as to the right of the mortgagee to obtain sequestration as against an owner or junior encumbrancer. But in the latter case, the Court is confronted with the primary question as to the relative legal rights of the parties contending for such rents under the applicable state law.

At page 26, appellants attempt to establish an analogy between the Livingston case and the case at bar by treating the order for maintenance of separate accounts as a sequestration for their benefit. We have already demonstrated that the order bears no such construction (pages 26 to 30 this brief).

An application in the bankruptcy court for the rents cannot, in any event, entitle the mortgagee thereto under the law of Oregon applicable in this case, because, as already demonstrated, the mortgagee's right to rents can only be perfected by obtaining the appointment of a receiver in foreclosure proceedings and the collection of rents by such receiver. This right was cut off by the intervention of bankruptcy; hence, application to the Bankruptcy Court for the rents collected by trustee in bankruptcy is a futile proceeding.

The case of **Bindseil v. Liberty Trust Co., 248 Fed. 112,** is not authority in this jurisdiction insofar as it held mortgagee entitled to the rents, because that case involved a **Pennsylvania mortgage,** which passes the legal title, right of possession and rents to the mortgagee (Appendix, p. 4).

In the **Bindseil** case the Court very clearly demonstrated that the rule would be different in jurisdictions like Oregon.

The Court said:

> "The cases which hold against the allowance to the mortgagee of rents arising out of mortgaged property after bankruptcy, are based upon the general rule of law, that a mortgage, though in form a conveyance of land, is merely a high security for the payment of a debt or the performance of some other condition (cases), and that, as between mortgagor and mortgagee, the mortgagor retains the title and has the right to all rents, issues and profits of the mortgaged premises, so long as he is in possession. In connection with this rule, **consideration is given the provision of the Bankruptcy Act, by which the trustee in bankruptcy acquires the mortgagor's possession of the mortgaged premises and succeeds to his title and rights. These cases hold in effect that until the mortgagee has reduced the mortgaged premises to his possession, or has attached or sequestered the rents (which, generally speaking, cannot be done after bankruptcy), the possession of the trustee is that of the bankrupt mortgagor,** and rents from the mortgaged premises, which, but for bankruptcy would belong to the mortgagor, after bankruptcy belong to the trustee by virtue of his title and possession, and are therefore applicable to debts due general creditors." (Cases.)

In the **Central Hanover Bank case, 99 Fed. (2d) 642 (3rd Cir.)**, the Court also dealt with a Pennsylvania mortgage (trust deed), (Appendix, p. 4), and for that reason held that when the 77B petition was filed, the mortgagee was the "virtual owner".

In **Florida Bank v. U. S., 87 Fed. (2d) 896 (5th Cir.)**, the mortgagee was in possession at the time of the filing of the re-organization proceeding. In Florida, a trustee under a trust deed has title for all purposes, together with all incidents of ownership (**Soutter v. Miller, 15 Fla. 625**).

In **Lincoln Bank v. Realty Associates, 67 Fed. (2d) 895,** the controversy over the rents was between the first and second mortgagees, the **trustee of the owner making no claim thereto.** The Court awarded the rents to the junior mortgagee on the authority of **Sullivan v. Rosson,** because he first took possession.

The principle of this line of cases is fatal to appellants' contention here, because it is based on the proposition that a lien on future rents only comes into existence upon taking actual possession of the property.

RESPONSE TO ARGUMENT RE: MORTGAGEE'S RIGHTS UNDER SECTION 77b.

At pages 31 to 39, appellants urge that a reorganization proceeding under 77b is the same as an equity receivership for the purpose of bringing

this case within the radius of the **Liberdar case, 74 Fed. (2d) 50.**

The case at bar originated with an involuntary petition in bankruptcy. While this proceeding was pending, the 77B proceeding was initiated, resulting in an order of liquidation, which, under the act, becomes an order of adjudication. If the 77B proceeding had been dismissed, adjudication would have followed, in any event, upon the involuntary petition.

In reality appellants' contention is an attempt to divorce section 77b from the rest of the Bankruptcy Act or to expunge the portion of Subdivision (c) (2) of that section which provides for the appointment of a trustee while the petition for reorganization is pending and that

> "every such trustee upon filing such bond, **shall have all the title** and shall exercise, subject to the control of the judge and consistently with the provisions of this section, **all the powers of a trustee appointed pursuant to Section 44 of this Act."**

The character of "title" which passes to the trustee is defined by section 70 of the Bankruptcy Act (11 U.S.C.A. Sec. 110) which provides

> "the trustee . . . . . shall in turn be vested by operation of law with the title of the bankrupt as of the date he was adjudged a bankrupt."

The "powers" which he may exercise are, of course, all of the powers conferred upon the trustee by all of the provisions of the Bankruptcy Act, and

those more particularly applicable to the case at bar are respectively Section 47a (2) (11 U.S.C.A. Sec. 75) which provides:

> "Such trustees as to all property in the custody or coming into the custody of the Bankruptcy Court shall be deemed vested with all the rights, remedies and powers of a creditor holding a lien by legal or equitable proceedings thereon, and also as to all property not in the custody of the Bankruptcy Court, shall be deemed vested with all the rights, remedies and powers of a judgment creditor holding an execution duly returned and satisfied."

and Section 67a (Title 11 U.S.C.A. Sec. 107a) which provides:

> "Claims which for want of record or **for any reasons** would not have been valid liens against the claims of the creditors of the bankrupt shall not be liens against his estate."

Section 77b (a) provides that in a reorganization proceeding the Court

> "shall have and may exercise all the powers, **not inconsistent with this section,** which a federal court would have had it appointed a receiver in equity of the property of the debtor."

Subdivision k of 77B provides, among other things, that upon the entry of an order of liquidation

> "a trustee shall be appointed as provided in Section 44. . . . Claims may be proved as provided by Section 57. . . . Dividends may be declared as provided in Section 65", and

substantially, all other provisions of the Bankruptcy

Act are made applicable thereby.

Subdivision 77B (o) provides:

> "In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition or answer was approved."

Giving effect to these provisions, the Supreme Court of the United States in **Callaghan v. R.F.C., 297 U.S. 464,** held that section 77B is "an integral part" of the Bankruptcy Act and must be read in connection with all other sections of the Bankruptcy Act.

In **Re: Fox Metropolitan Playhouses, Inc., 74 Fed. (2d) 722 (2d Cir.),** the Court held that when a 77B proceeding is filed,

> "Then for all purposes the bankrupt's estate is in the same status as when a voluntary petition is filed in the ordinary bankruptcy proceeding."

It is true that Sec. 77B confers upon the Bankruptcy Court all the jurisdiction formerly exercised in equity receiverships, but **there was added** thereto the provisions of the Bankruptcy Act which place the estate in status quo and cut off the right to affect a change of position by perfecting liens and the like. It also takes the title to the property out of the debtor and places it in the trustee so that dur-

ing the consideration of the reorganization plan, no one could acquire rights that were not fixed at the date of the filing of the petition. This was not true under the equity receivership; it did not prevent the perfection of liens after the commencement of the proceeding.

Justice Cardozo did not, in the Duparquet case, even intimate that mortgagees are in the same position in reorganization proceedings under 77B as they occupied in the former equity receiverships. He only decided that a receivership in foreclosure proceedings was not an act of bankruptcy.

It is not true, as urged (page 37) that Sec. 77B (insofar as it permits temporary restraining of foreclosure proceedings) imposes any greater hardship on a mortgagee than did the Bankruptcy Act prior to the adoption of 77B. The Bankruptcy Court could, in its discretion, enjoin further prosecution of pending foreclosure proceedings or enjoin commencement of any foreclosure proceedings (**Isaacs v. Hobbs, 282 U.S. 734**). The power to restrain foreclosure proceedings under 77B is likewise discretionary.

In **Continental Illinois National Bank & Trust Co. v. Chicago, etc. Co., 294 U.S. 648**, the Court held that Congress had the power, under the constitutional provisions relating to bankruptcy, to provide for delay in the prosecution of foreclosure proceedings, by injunction or otherwise and that such provisions **do not violate the Fifth Amendment to**

the United States Constitution.

The contention (page 37) that the debtor owned practically no assets other than the mortgaged premises is without foundation. The debtor had a great many properties (encumbered and unencumbered, mortgages and personal property.

It is urged that "fairness and equity" require that the rents should be surrendered to the mortgagees. The factors creating these alleged equities are not made apparent. What the mortgagees ask the Court to do is to make non-applicable to them the provisions of the Bankruptcy Act.

The extent to which "equitable principles" will be employed in bankruptcy cases was clearly defined by this Court in **Re: Judith Gap Commercial Co., 5 Fed. (2d) 307-309 (9th Cir.)**. The Court there said that:

> ". . . . though bankruptcy proceedings are equitable in their nature and must be carried on as such, nevertheless they are to be administered in accord with the Bankruptcy Act and general orders, **and not by virtue of any broad unlimited equity power**" (cases).

In **Smith v. Chase Nat. Bank, 84 Fed. (2d) 608,** 615 (8th Cir.), the Court held:

> "It (the court) has not, however, plenary jurisdiction in equity, **but is confined, in the application of the rules and principles of equity, to the jurisdiction conferred upon it by the provisions of the Bankruptcy Act** (11 U.S.C.A., Sec. 1 et seq.), reasonably interpreted" (cases).

RESPONSE TO ARGUMENT THAT DENIAL OF MORTGAGEES' CLAIM TO RENTS WILL VIOLATE FIFTH AMENDMENT.

The entire argument (presented, pp. 39 to 43), is predicated upon the erroneous assumption that the mortgagees had **existing liens** on rents at the time of the commencement of the bankruptcy proceedings. They confuse the **existing lien** upon the **land**, with the **contract for a lien** (covenant pledging future rents), which did not and could not ripen into a lien until mortgagees had either taken possession or procured the appointment of a receiver who collected the rents. The trustee in bankruptcy took title subject to the lien on the land, **but not subject to any lien on future rents** because there was no lien in existence. The Bankruptcy Act only cut off the right to perfect a lien **thereafter.**

In passing upon the various provisions of the Bankruptcy Act, including the recent reorganization acts, the Supreme Court of the United States has made a clean-cut distinction between **"property and property rights"** on the one hand, and **"contract rights"** on the other, and has held definitely that impairment of contract rights does not violate the United States Constitution for the obvious reason that there is no such prohibition in the United States Constitution. When the Constitution of the United States granted Congress the power to legislate with respect to bankruptcy, it necessarily car-

ried with it the power to effect contract rights. Provisions granting discharge, compelling creditors to accept a composition upon the consent of 50% of the creditors, substitution of a claim for three years' rent for the contract right to recover for anticipatory breach of a lease for the entire unexpired term, are some of the instances in which the power of Congress to impair contracts was recognized, and the validity sustained.

In **Hanover National Bank v. Moyses, 186 U.S. 181**, it was held:

> "The grant to Congress involves the power to impair the obligation of contracts, and this the states were forbidden to do."

In **Kuehner v. Irving Trust Co., 299 U.S. 445, 57 S. Ct. 298** (lease case), the Court held:

> "As pointed out in the case last cited there is, as respects the exertion of the bankruptcy power, a **significant difference between a property interest and a contract, since the Constitution does not forbid impairment of the obligation of the latter.** The equitable distribution of the bankrupt's assets, or the equitable adjustment of creditors' claims in respect of those assets, by way of reorganization, may therefore be regulated by a bankruptcy law which impairs the obligation of the debtor's contracts. Indeed every Bankruptcy Act avowedly works such impairment."

The same doctrine was announced and elaborated on in **Wright v. Vinton Branch of Mountain Trust Bank, 300 U.S. 440**, and **Continental Illinois Nat'l**

Bank & T. Co. v. Chicago, etc. Co., 294 U.S. 648.

It is well settled that all contracts are made subject to constitutional power to legislate on the subject of bankruptcy.

In **Wright v. Union Central Life Ins. Co., 304 U. S. 502, 516,** the Court said:

> "The mortgage contract was made subject to constitutional power in the Congress to legislate on the subject of bankruptcies. Impliedly, this was written into the contract between petitioner and respondent. '**Not only** are **existing laws read into contracts** in order to fix obligations as between the parties, but the reservation of essential attributes of sovereign power is also read into contracts as a postulate of the legal order'."

Appellants argue (page 40) that if the Bankruptcy Act is construed so as to prevent the mortgagees from obtaining the rents collected by the trustee in bankruptcy, it would be unconstitutional under **Louisville Bank v. Radford, 295 U.S. 555.**

In states like Pennsylvania the Bankruptcy Act would not affect mortgagee's right to rents because he is owner of the property and of the rents accruing therefrom. This right is protected by the Act. But in Oregon the mortgagee is not the owner of the property or the rents. Hence the Bankruptcy Act does not deprive him of anything. **The Act merely fixes the status quo.**

In **Remington on Bankruptcy, Vol. 1, Sec. 6, page 28,** the author points out:

> "Property that will pass to the trustee in one State may not, because of diversity of laws, pass in another State; as, for instance, unrecorded conditional sales contracts are void as to creditors in some States and the property covered by them passes to the trustee; in other States they are not void and the same class of property does not pass; yet the law operates uniformly because the creditors still get all the property they would have had had there been no bankruptcy law." (Citing Hanover Nat'l Bank v. Moyses, 186 U.S. 181, 22 S. Ct. Rep. 857).

The first Frazier-Lemke Act was not held invalid on the "sole" ground that it deprived the mortgagee of the right to collect the rents during the pendency of the period of time provided for in the Act. The Supreme Court, in passing upon the validity of the amended Frazier-Lemke Act in **Wright v. Vinton Branch of Mountain Trust Bank, 300 U.S. 440, 456, 57 S. Ct. 556, 559,** said:

> "The original Frazier-Lemke Act was there held invalid solely on the ground that the bankruptcy power of Congress, like its other great powers, is subject to the Fifth Amendment; and that, as applied to mortgages given before its enactment, the statute violated that Amendment, since it effected a substantial impairment of the mortgagee's security. The opinion **enumerates five important substantive rights** in specific property which had been taken. **It was not held that the deprivation of any one of these rights would have rendered the Act invalid**, but that the effect of the statute in its entirety was to deprive the mortgagee of his property without due process of law."

The withholding of the right to collect the rents

was only one of the five rights enumerated in the Radford case. The Court held clearly that the withholding of that right alone **would not** render the act invalid. It was the withholding of all of the five rights that rendered the act invalid. The cumulative effect was to **deprive the mortgagee of the security itself.**

In the case at bar appellants had no lien on rents to be retained. **They want the Court to perfect a lien for them which they did not have when the bankruptcy petition was filed.**

RESPONSE TO APPELLANTS' APPLICATION OF LEGAL PRINCIPLES TO FACTS OF THE PRESENT CASE.

At pages 44 to 47, appellants attempt to apply the law theretofore discussed to this case, but assume facts not suported by the record.

1. The order for separate accounts was not a sequestration for the benefit of these mortgagees.

2. Mortgagees did not participate in these bankruptcy proceedings at the Master's hearing. They **appeared specially.** They did not ask for and were not granted any relief at that time, or at any time thereafter, except the leave to foreclose their mortgages in other tribunals.

3. They did not assert claims to rents at the Master's hearing held in August, 1934, or at the time that Judge McNary made the order for the mainte-

nance of separate accounts.

4. The Court did not require that separate accounts be kept of receipts and expense as to mortgaged properties. The order was made to include all properties, **encumbered or unencumbered,** which clearly precludes the idea that this order was intended as a sequestration for the benefit of these particular mortgagees.

5. There was no sequestration for the mortgagees' benefit prior to bankruptcy.

6. There is no foundation in the record for appellants' statement (p. 46) that they appeared before the Special Master, asserted their rights as mortgagees "and obtained an order that the rents from each of the mortgaged properties be kept separate and apart, etc." Neither the order of Judge McNary nor the Master's recommendation was made upon the motion of the mortgagees.

RE: CLAIM OF PORTLAND TRUST AND SAVINGS BANK

As to the Bank appellant, Judge Fee held (R. 129):

> "No distinction can be drawn in the case of the mortgages held by the Portland Trust & Savings Bank where foreclosure was commenced in the state court prior to the filing of the involuntary petition. The state court did not appoint a receiver in that case although petitioned to do so. Instead it recognized the possession of the Guaranty Trust Company and since it had

> jurisdiction of the cause and the parties gave a direction to the Guaranty Trust Company **in personam** to pay the rentals monthly as collected and less an allowance for expenses into court for application upon the agreement. So far as that direction was obeyed it constituted a valid seizure of the rents. But the Court did not lay its hands on the res or have possession of the property through a receiver, or otherwise. The possession of the realty by the Guaranty Trust Company was expressly recognized. No lien was thereby established upon rents subsequently accruing or paid. The court could only have enforced the order by contempt proceedings and after the appointment of a trustee in this court who took possession had no power over rents accruing in the future or moneys in the hands of the bankrupt."

The state court retained no supervision over the operation, management, or control of the property; it imposed no charge upon future rents; it did not restrain or enjoin assignment of the rents or conveyance of the property pendente lite, and it was not binding upon any successors of the owner, whether he be grantee, trustee in bankruptcy, or an intervening attaching creditor.

Under the Oregon law as we have demonstrated, to perfect a lien upon rents, the mortgagee must have unequivocal possession, either by consent of the owner or through a receiver who actually takes possession and collects the rents. The lien attaches to the rents thus collected. The order made by the state court did not give the mortgagee that character of possession which was requisite to the perfection of

the lien. The very fact that the bankruptcy trustee was able to and did obtain peaceful possession negatives possession in the mortgagee.

The case of **Hitz v. Jenks, 123 U.S. 297**, cited by appellants, does not support the contention that the state court order was the equivalent to prior possession. The rents, which were the subject of controversy, were collected by Keyser (representative of mortgagee). He was **in actual possession** of the property which was turned over to him by the owner. Part of the rents were collected by him while he was in possession under the surrender, and part while acting in the capacity of a **receiver appointed by the Court** in that litigation. The Court dealt with the two funds separately; first

> "for rents received with the consent of Hitz" (owner),

and second, with respect to

> "rents received by Keyser under his appointment as receiver by the decree of the Court and paid by him into the registry of the Court."

In the case at bar the owner never parted with possession, and there was no receiver prior to commencement of the bankruptcy proceeding.

Capital is made out of the fact that some rent was paid into the state court by the bankrupt after the petition in bankruptcy was filed, and that two month's rent, which was collected by Twining as receiver, was paid over to Mr. Kaste, the bankrupt's attorney. This, together with other rentals collected

by Kaste subsequent to the filing of the bankruptcy petition was later turned over to the trustee in bankruptcy upon order of the Court. The payment of a few months' rental to the state court was on an ex parte order taken by bankrupt's attorney. It was not made upon notice to or consent of any trustee or receiver in bankruptcy. **When the trustee did raise a question in respect to the payment of such rentals, the Court directed Mr. Kaste, who had been collecting the rents, to surrender them to the trustee in bankruptcy,** which he did (R. 13).

It is well settled that no one can surrender property over which the Bankruptcy Court has jurisdiction. A trustee in bankruptcy cannot give away any assets of the estate, and if he does so, the recipient of such assets will acquire no title thereto. **Isaac v. Hobbs, 282 U.S. 734.**

Pending the appointment of a trustee, if the bankrupt remains in possession, he is, by operation of law, the trustee of the title for the benefit of the creditors (Johnson v. Colber, 222 U.S. 538). Hence, neither the bankrupt nor its attorney had any right to pay over any rents to the state court, and those rents are recoverable by the trustee in bankruptcy subsequently appointed.

Some capital is also made out of the fact that the trustee purchased a certificate of deposit in the Bank of California. This was not done pursuant to any order of the Court; it was without authority and in violation of the Bankruptcy Act, which requires

all of the bankruptcy funds to be deposited in a duly appointed and qualified depository. Upon this unauthorized act, appellants' counsel assert that this money was "impounded" in the Bank of California for its benefit.

It goes without saying that the trustee could not, of his own account, take funds which are the property of the estate and impress it with a trust in favor of someone else, for that would be the equivalent of surrendering jurisdiction over the fund in violation of the Bankruptcy Act (Isaacs v. Hobbs, supra).

Appellants' counsel refer to this money repeatedly as the "trust fund".

There is no order of Court in the record authorizing the creation of any trust fund, nor is there any evidence of the existence of a "trust account" at the Bank of California. The whole argument as to the existence of a "trust fund" is imposed upon an inadvertent use of the term by one of the writers of this brief. It was an inaccurate reference to the certificate of deposit.

Neither the Special Master nor the District Judge treated this certificate of deposit as a trust fund. The Master's findings of fact with respect to the rentals from these two apartments is to be found at page 87 of the record. He said:

> "Such net rentals and income for the period subsequent to May 11, 1934, was collected by said John W. Kaste and retained by him until

> after the appointment of C. W. Twining as trustee in this proceeding. Thereafter said John W. Kaste, upon the order of this court, paid the accumulated net income and rental in his hands to said C. W. Twining as trustee. **From that time on such net rentals and income have been received by the trustee in this proceeding."**

This was the finding upon which the Master made the report and which was reviewed by Judge Fee upon the exceptions to the report. It is obvious that the unlawful purchase of the certificate of deposit was not considered a factor in determining the question here involved, either by the Master who held in favor of this mortgagee, or by the District Judge who held against it.

The case of **Re: Burdick, 56 Fed. (2d) 288,** cited by the Bank, does not support the contention that the state court order was equivalent to prior possession, because the owner had by written consent, prior to bankruptcy, permitted mortgagee

> "To go into possession of the premises and in the same paper assigned to it the rents thereafter accruing . . . . ."

The mortgagee also gave written notice to the tenants "that mortgagee was in possession".

The case did not involve any controversy as to rents accruing after bankruptcy collected by the trustee.

It is argued (p. 55) that sequestration is not a technical conception. In Oregon the statute fixes the method of perfecting a lien upon future rents.

We are not concerned with the question as to what would constitute sequestration in other jurisdictions.

In the two **Kansas cases, Farmers Union v. Sullivan and Hall v. Goldsworthy,** cited by appellants, the controversy involved rents **in the possession of the mortgagee.** Here the controversy is over rents in the possession of the trustee-owner.

In the **Farmers Union case,** the Court pointed out:

> "Here we have the **owner or mortgagor joining the mortgagee** in making a stipulation with the plaintiff agreeing to the payment of the rent to the mortgagee as the agent of the court. . . . There is no need for a judicial proceeding when the mortgagor voluntarily consents to the mortgagee's obtaining possession of the rents even as an agent of the court."

In the **Hall case** the Court concluded by saying:

> "In view, however, of the agreement made between the parties (referring to the agreement for possession after the foreclosure proceeding was commnced), the court holds that the rents in the hands of Glasgow should be paid to the appellant (mortgagee)."

The Kansas court in the two cases cited distinguished those cases from cases similar to the one at bar and cited numerous authorities supporting the distinction.

RESPONSE TO APPELLANTS' CONTENTION "MORTGAGEES' REMEDY IN BANKRUPTCY COURT NOT IMPAIRED BY STATE LAW".

Under this title it is argued that appellants would have been entitled to appointment of a receiver prior to bankruptcy.

This is wholly irrelevant. The fact remains that a receiver was not appointed; hence, the lien on future rents was never perfected.

We take issue with the statement of appellants' counsel (p. 59) that there is "admittedly" ample ground for the appointment of a receiver if bankruptcy had not intervened. None of the petitions show (a) insolvency of the obligors or (b) insufficiency of the security. The Investors Syndicate petitions show value of security at that time was in excess of indebtedness (R. 49). A court of equity would be without jurisdiction to appoint a receiver because the mortgagee had an adequate remedy at law.

We take issue with appellants' statement (p. 67) that practically all of the cases they cite arose in jurisdictions where the law governing mortgages was the same as in Oregon. Every decision relied on by appellants was based upon the law of a state in which the mortgagee is the owner of the title, with the incidental right of possession and rents. (See summary of the laws in the various states involved in the cases cited by appellants, Appendix, page 1).

RESPONSE TO CONTENTION THAT 1927 AMENDMENT IS APPLICABLE TO MORTGAGES EXECUTED PRIOR TO ITS ADOPTION

The 1927 amendment was not a "validating act" or a "curative act". It was not enacted to validate transactions deemed for technical reasons invalid prior thereto.

The case of **Gross v. U. S. Mortgage Co., 108 U. S. 477,** cited by appellants (p. 76) is a typical illustration of a validating act. Prior to 1875, in Illinois, a foreign corporation could not take mortgages on real property. In 1875 an act was passed which provided:

> "And any such corporation **that may have invested** or lent money, as aforesaid, **may have the same rights** and powers for the recovery thereof . . . as private persons, citizens of this State."

This statute expressly made enforcible mortgages made prior to its adoption.

The Amendment in the case at bar does not, **in terms**, validate any prior transactions. We are concerned, therefore, with the question

(a) does the language embrace mortgages made prior to the enactment?

(b) If it does, is it invalid as an impairment of vested rights?

The title of the 1927 Act reads "To amend section 335 Oregon Laws relating to **possession of mortgaged real property**".

In Michigan there was a statute of the same import as 5-112 Oregon Code prior to the amendment. In 1925 there was adopted a statute similar to the amendment in the case at bar. The Michigan Supreme Court held several times that the amendment **did not apply to mortgages executed prior to its adoption.**

In **Detroit Trust Co. v. Lipsitz, 249 N.W. 892 (Mich.)**, the Court said:

> **"Inasmuch as the mortgage was given prior to the effective date of Act No. 228, Pub. Acts of 1925, the assignments of rents clause is not enforceable."**

The same rule was applied in **American Trust Co. v. Michigan Trust Co.**, 248 N.W. 829; **Union Guardian Trust Co. v. Commercial Realty Co.**, 251 N.W. 786; **Freedman v. Massachusetts Mut. Life Ins. Co.**, 81 Fed. (2d) 698 (6th Cir.), (applying Michigan law).

The Oregon Supreme Court had the matter before it in **State ex rel. Nayberger v. McDonald, 128 Ore. 684.** The trial court appointed a receiver after the amendment upon a mortgage executed prior to the amendment. It was contended there that the amendment was applicable to mortgages executed prior thereto. The Court held the appointment void and quoted only the statute as it existed prior to

the amendment. Believing that the Court had overlooked the amendment, the matter was specifically called to its attention by petition for rehearing. The petition was denied without any opinion, and we believe that it is a fair interpretation of the court's ruling that it deemed the amendment to be inapplicable to mortgages executed prior to its adoption.

Thereafter the owner sued for damages sustained by reason of the void receivership. It was again urged that the 1927 amendment was applicable to the mortgage, but the Court adhered to its former decision and said (6 P. (2d) 228):

> "We held that the order appointing a receiver and naming Guild was void because a receivership of that character was not authorized by section 32-702 Oregon Code **1930"** (now 5-112).

Although the Court did not, in express language, refer to the 1927 amendment, the effect of the decision is to hold that the 1927 amendment was not applicable to a mortgage executed prior to its adoption.

In **Libby v. Southern Pacific Co., 109 Ore. 449,** 452, the Court held:

> "The doctrine of the case is that no act will be held to have a retrospective effect **unless** the intention in that respect is **clearly apparent in the statute itself.** On the contrary, **if it is fairly possible to restrain the operation of the statute so as to be prospective, that course will be adopted by the courts."** (Citing cases.)

In **Seton v. Hoyt, 34 Ore. 266, 279,** the Court held:

> ". . . . . it is a general rule that a statute was intended to operate **prospectively only,** unless a purpose to give it a retrospective force is declared **by clear and positive command,** or is to be inferred by necessary and unavoidable implication from the language of the act, taken in its appropriate signification, and construed in connection with the subject-matter and the occasion of the enactment, **admitting of no reasonable doubt,** but precluding all question as to such intention." (Citing numerous cases.)

The rule of construction laid down in the foregoing authorities are particularly applicable **to expository laws** for the reasons assigned in the following cases.

In **Virginia Coupon Cases, 25 Fed. 647,** the Court said:

> "So far as it undertook, in declaring the true intent and meaning of a previous statute, to give that meaning a retrospective operation, it was **nugatory. It is not competent for the legislative department of government to declare the meaning of previous statutes for such a purpose. That is the province of the courts.** If the new statute declares the law to mean what the courts declare it to mean, then it is useless. **If it undertake to give the law a meaning different from that given by the courts, then it is void. To declare what the law is or has been is a judicial function. To declare what it shall be, is legislative. Cooley, Const. Lim. 94."**

In **Richardson v. Fitzgerald, 109 N.W. 866,** the Court said:

> **"Certainly the lawmakers had no purpose of instructing this court with reference to the construction of the original statute. As everyone**
>
> **knows, it is the province of the legislature to enact, of the judiciary to expound, and of the executive to enforce, the laws, and any direction by the legislature that the judicial function shall be performed in a particular way is a plain violation of the Constitution. . . . . Expository legislation is so uniformly condemned by the courts that we need cite no more than a few of the numerous decisions with our approval of the principle** (cases). **The legislature may say what the law shall be, not what it is or has been, and this it is very clear was its intention in enacting the amendment.** This disposes of appellant's contention with respect to the curative effect of the amendment."

See **Lewis' Sutherland Statutory Construction. Volume 2, page 635.**

Judge Fee did not unqualifiedly hold that the amendment was retroactive as asserted by appellants (p. 70). He held that the amendment could be held applicable to pre-existing mortgages only if it was construed (R. p. 128) so that the proviso "did not change the body of the statute which denies to a mortgagee any remedy for obtaining possession of the mortgaged premises; that the mortgagor may still refuse possession, retain the rents and profits and will not be liable therefor in accordance with Teal v. Walker; that the law is unchanged that the mortgagor still has the right of possession although rents are pledged; and that such pledge "may be enforced **strictly in accordance with the statute"**

upon equitable principles **"if full protection be given to intervening rights".**

"So construed", said Judge Fee, "the proviso is valid since the agreement to assign the rents accruing after default was not illegal when made and since the proviso grants remedies **narrowly circumscribed."**

When the trustee in bankruptcy became the owner and succeeded to the rights of a creditor holding a lien by attachment under Sec. 47 and all right to perfect liens was cut off by Sec. 67, the trustee acquired vested rights to possession and rents until foreclosure and sale.

CONCLUSION

The opinion rendered by Judge Fee is a clear, concise, and accurate statement of the law applicable to the case at bar, and the order appealed from should be affirmed.

Respectfully submitted,

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APPENDIX

Digest of the law of several states as to the respective rights of mortgagor and mortgagee from Jones on Mortgages, 8th Ed., Vol. 1, Sections 18 to 66.

SECTION 19 (18).—ALABAMA

"In Alabama a mortgage passes to the mortgagee, as between him and the mortgagor, the estate in the land. It confers something more than a mere security for a debt: it confers a title under which the mortgagee may take immediate possession, unless it appears by express stipulation, or necessary implication, that the mortgagor may remain in possession until default. After the law day, the legal estate is absolutely vested in the mortgagee, who may forthwith maintain ejectment, and the mortgagor has nothing left but an equity of redemption. A conveyance by the mortgagee will pass the legal title, though the debt be not assigned. Nothing but payment, or a release of the mortgage, or a reconveyance, can operate in a court of law to revest the title in the mortgagor; and it is questioned whether payment alone after the law day is sufficient . . . . It is held that a partial payment after default and after the law day does not operate to divest the mortgagee's title. . . . . .

After the legal title has vested in the mortgagee by reason of the condition being broken, he may convey the premises to another, even though not in possession. The mortgagor still has an equity of redemption which the courts of law will not notice, but which may be asserted and protected in equity until duly foreclosed."

SECTION 29—ILLINOIS

"While the mortgagor is the legal owner of the mortgaged premises against all persons except the mortgagee, the mortgagee, as against the mortgagor, is held to be the owner of the fee, and entitled to all the rights and remedies which the law gives to such owner. . . . . .

Upon breach of the condition, the mortgagee has the legal title, and may bring his action without giving the party in possession any notice to quit. . . . . The mortgagee may pursue all his remedies at the same time: he may proceed against the debtor personally; against the property by bill in chancery for a strict foreclosure, or for a foreclosure and sale; or, when the debt is still due, by scire facias; and, **he may bring ejectment for the possession**, or make peaceable entry (many cases are cited)."

SECTION 37—MASSACHUSETTS.

"In Massachusetts the English characteristics of a mortgage are retained. **It confers upon the mortgagee a legal estate and the right of possession.** . . . . Hence it is that, as between mortgagor and mortgagee, the mortgage is to be regarded as a conveyance in fee; because that construction best secures him in his remedy and his ultimate right to the estate, and to its incidents, the rents and profits. . . .

As between the parties, the mortgage is regarded as a conveyance of the fee for the protection of the rights of the mortgagee, and entitles him to immediate possession. . . . . The mortgagee may, even before breach of condition, maintain ejectment and oust the mortgagor."

SECTION 41—MISSOURI

"In Missouri a mortgage is only a security for a debt, and remains so even after a condition broken; but upon default in the payment of the debt **the mortgagee may maintain ejectment, because he is then in law regarded as the owner of the estate;** but the legal title vests in him only for the purpose of protecting his debt. By a mortgage, or a deed of trust in the nature of a mortgage, the legal title, after condition broken, passes to the mortgagee or trustee. The addition of a power to sell, without judicial proceedings to foreclose, can not avoid the legal effect of the grant. In the case of an absolute deed intended as a mortgage, it is held that the legal title is conveyed, and the grantor has only an equity.

Where a mortgage debt is payable by instalments, the condition is broken by nonpayment of any one of them, and **the mortgagee may thereupon enter or bring ejectment.** . . . . (citing many cases)."

SECTION 46—NEW JERSEY

"In New Jersey the nature of the mortgage as a conveyance of an estate to the mortgagee in fee simple, subject to be defeated by the performance of the condition, remains as it was at common law, with the modification that the mortgagee can not enter immediately as at common law, but only upon breach of the condition."

In the footnote the author quotes from **Woodside v. Adams, 40 N.J.L. 417, 422,** where the court says:

"The legal estate of the mortgagee, after breach of condition, has all the incidents of com-law-law title, for the purposes of an action of ejectment." (Cite other N.J. cases showing right of entry.)

SECTION 51—OHIO

"In Ohio a mortgagee is regarded as holding the legal title to the estate during the continuance of the mortgage, ... After condition broken, the legal title is in the mortgagee, and he may recover possession by an action of ejectment."

SECTION 53—OREGON

"In Oregon a mortgage does not convey a title, but only creates a lien. The mortgagee's interest is of a personal nature, and the lien is similar in effect to that created by an ordinary judgment. **By statute** a mortgagor can not against his will be divested of possession of the mortgaged premises, even upon default, without a foreclosure and sale. He retains the right of possession and the legal title."

SECTION 54—PENNSYLVANIA

"In Pennsylvania a mortgage passes to the mortgagee the title and right of possession to hold till payment be made. He may enter at pleasure, and take actual possession. His estate is conditional, and ceases upon payment of the debt; but until the condition is performed, both his title and his right of possession are as substantial and real as though they were absolute. As between the parties, the mortgage transmit the legal title to the mortgagee, and leaves the mortgagor only a right to redeem. . . . .

It is well settled that a mortgagee or his assignee may maintain ejectment and recover possession of the mortgaged property before the condition is broken, unless there be a stipulation in the instrument to the contrary. 'For some purposes a mortgage is something more than a mere security for a debt. It is a pledge of a specific property. It gives to the creditor the exceptional remedy of ejectment."

SECTION 59—TEXAS

"A mortgage is but a security, and the title remains in the mortgagor, subject to be divested by foreclosure. In this respect a deed of trust is held not to differ from a mortgage; . . . . . The same rule applies to an absolute deed given as security, ... And since the mortgagor remains the real owner of the land is entitled to the possession, after as well as before breach of condition, the mortgagee can not dispossess him by an action of trespass to try title."

Quotations from authorities re Oregon Law, Page 7 of this brief.

In **Teal v. Walker, 111 U.S. 242-248,** the Court construed this statute and held:

> "We believe that the rule is, without exception, that the mortgagee is not entitled to demand of the owner of the equity of redemption the rents and profits of the mortgaged premises until he takes actual possession."
>
> . . . . . .
>
> "Chancellor Kent states the modern doctrine in the following language: 'The mortgagor has a right to lease, sell, and in every respect to deal with the mortgaged premises as owner so long as he is permitted to remain in possession, and so long as it is understood and held that every person taking under him takes subject to all the rights of the mortgagee, unimpaired and unaffected. Nor is he liable for rents; and the mortgagee must recover the possession by regular entry by suit before he can treat the mortgagor, or the person holding under him, as a trespasser'."
>
> . . . . . .
>
> "The authorities cited show that, as the defendant in error took no effectual steps to gain possession of the mortgaged premises, he is not entitled to the rents and profits while they were occupied by the owner of the equity of redemption.
>
> The case against the right of the defendant in error to recover in this case the rents and profits received by the owner of the equity of redemption is strengthened by section 323, c. 4. tit. 1, Gen. Laws Or. 1843-1872 (now 5-112 Oregon Code) which declares that 'a mortgage of real property shall not be deemed a conveyance

so as to enable the owner of the mortgage to recover possession of the real property without a foreclosure and sale according to law'. This provision of the statute cuts up by the roots the doctrine of Moss v. Gallimore, ubi supra, and gives effect to the view of the American courts of equity that a mortgage is a mere security for a debt, and establishes absolutely the rule that the mortgagee is not entitled to the rents and profits until he gets possession under a decree of foreclosure. For if a mortgage is not a conveyance, and the mortgagee is not entitled to possession, his claim to the rents is without support. **This is recognized by the supreme court of Oregon as the effect of a mortgage in that state.**

. . . . . .

The case of the defendant in error cannot be aided by the stipulation . . . . that Goldsmith and Teal would, upon default . . . . deliver to Hewett, the trustee, the possession of the mortgaged premises. That contract was **contrary to the public policy of the state of Oregon,** as expressed **in the statute just cited, and was not binding on the mortgagor** or his vendee, and, although not expressly prohibited by law, yet, like all contracts opposed to the public policy of the state, it cannot be enforced." (Boldface emphasis by writer.)

A petition to the Bankruptcy Court for rents collected by the trustee (owner) is in all essential respects the same as an action by a mortgagee against a mortgagor (owner) for rents collected by him. It presents the identical question.

The bare circumstance that the claim must be litigated in the Bankruptcy Court does not change the contractual or legal rights of the parties. It is

still a controversy over the rents between the mortgagee on the one hand and the owner of the fee in possession on the other hand, and such controversy must be determined by the legal status of the parties as fixed by the law of the State of Oregon.

In **Thomson v. Shirley, 69 Fed. 484 (District of Oregon), aff'd Couper v. Shirley, 75 Fed. 168** (9th Cir.), the mortgage contained a provision that in case foreclosure proceedings were instituted, a receiver may be appointed to collect the rents and profits and apply them on the mortgage. Foreclosure proceedings were commenced, and a receiver was appointed ex parte. The Court held:

> "Under this statute (referring to 5-112 Ore. Code prior to amendment), the mortgagee is not entitled to the rents and profits before actual possession, even when the mortgagor covenants in the mortgage to surrender the mortgaged property on default in payment of the debt, and nevertheless refuses to deliver it after default. Teal v. Walker, 111 U.S. 242, 4 Sup. Ct. 420."

In **Savings & Loan Soc. v. Multnomah County, 169 U.S. 421**, the Court held:

> "By the **law of Oregon**, indeed, as of some other states of the Union, a mortgage of real property does not convey the legal title to the mortgagee, but creates only a lien or incumbrance as security for the mortgage debt; and the right of possession as well as the legal title, remains in the mortgagor, both before and after condition broken, until foreclosure." (Citing cases.)

In **State ex rel. Nayberger v. John F. McDonald, 128 Ore. 684, 695, 696—274 Pac. 1104,** decided after amendment, the Court held:

> "The statutes of this state provide, among other matters, that a mortgage shall not be deemed as a conveyance so as to enable the owner or mortgagee to recover possession of any real property without foreclosure and sale according to law, and it has been repeatedly held that the **mortgagee has no right to cut off the possession of the mortgagor** to the mortgaged premises **until such time as his title is divested by a perfect foreclosure.** This is law everywhere where statutes similar to those of this state are in force (cases). . . . . So we are clearly convinced that neither the complaint nor the affidavit of Guild were sufficient to authorize the court to appoint a receiver, and that the appointment was absolutely void."

In **McKinney v. Nayberger, 138 Or. 203, 215—2 Pac. (2d) 1111—6 Pac. (2d) 228-229,** decided after amendment, the Court held:

> "Our decision pointed out that the order for the receivership disregarded the **statutory limitations** upon the court's authority to appoint a receiver . . . . . .
>
> In State ex rel. Nayberger v. McDonald, 128 Or. 684 (274 P. 1104), we held that the order appointing a receiver, and naming Guild, was void because a receivership of that character was not authorized by section 32-702, Oregon Code 1930 (now 5-112 Oregon Code).
>
> . . . . . .
>
> Since we are of the opinion that the order authorizing the receivership **exceeded the express limitations of our statutes** authorizing such re-

lief, we remain content with the conclusion previously expressed that the order is subject to collateral attack."

In **Schleef v. Purdy, 107 Ore. 71, 76,** the Court quoted from **Sellwood v. Gray, 11 Or. 534, 537,** as follows:

"The mortgage works no change of ownership in the property. It is still the property of the mortgagor, **in law and in equity; is liable for his debts; may be sold under execution, conveyed or devised; is subject to dower, or may be again mortgaged, as any other estate in land. Nor do any of the qualities or incidents of an estate in land attach in the mortgagee;** he has but a lien upon the land as a security for repayment, and **which cannot operate to affect the possession** of the mortgagor without his consent, or to transfer his estate in the land, except after default, and by force of a judicial sale under a decree of foreclosure."

Quotation from additional cases in support of the contention that mortgagee's right to perfect liens upon further rents was cut off by the intervention of bankruptcy. Page 26 of this brief.

In re Foster, 9 Fed. Cas., p. 523, Case No. 4963, aff'd 9 Fed. Cas., p. 572, Case No. 4982, the trustee in bankruptcy came into possession of mortgaged premises and collected rents. Thereafter mortgagee, who had foreclosed his mortgage, petitioned the bankruptcy court for an order to turn over the rents collected and for payment of taxes which the mortgagee had paid. The court held;

> "I do not at present see how any proceeding, no matter when taken, can entitle a mortgagee to collect the rents of mortgaged **property,** which had **passed into the possession of an assignee in bankruptcy before the rents became due.** An application by a mortgagee for the appointment of a receiver to collect, for his benefit, rents of the mortgaged premises accruing during the pendency of a foreclosure suit is not based upon any absolute right.
>
> It is, in legal effect, a proceeding to acquire immediate possession of the mortgaged premises, and it may be defeated by the intervention of superior equities, or by the collection of the rents by the mortgagor. It is addressed to the discretion of the court; when granted, the rents secured thereby arise from the possession of the property **at the time the rent became due,** such possession being acquired by means of a receiver.
>
> But if some proceeding, intended to divert the rents from the hands of the assignee, could

> avail when taken in time, it seems clear that there remains no ground on which to base a claim like the present, where a second mortgagee petitions to be paid rents which, before the filing of his petition, had been collected by the **assignee in bankruptcy, as owner in possession** of the mortgaged property at the time they became due. Moneys so collected by an **assignee in bankruptcy** are assigned by the law to be distributed equally among all the creditors, unless shown to be subject to some prior specific lien."

In **Alexander v. Smithe Machine Co., 143 N.E. 321-2 A.B.R. (N.S.) 500 (Mass.)**, a mortgagee attempted to perfect a lien of a chattel mortgage, which was invalid by reason of the failure to record, by taking possession of the property **after the filing of the bankruptcy petition.** The Supreme Court of Massachusetts held:

> "The defendant's title in mortgage **could not be perfected** by his taking possession of the machines **after** the filing of the petition in bankruptcy and before the adjudication, since by the amendment of the Bankruptcy Act (the Act of June 25, 1910)—
>
> > 'The trustees have the rights and remedies of a lien creditor or a judgment creditor as against an unrecorded transfer. The estate was in custodia legis from the filing of the petition, and the title of the trustee related back to that date." (Citing cases.)

In **Goldman, Beckman & Co. v. Smith, 2 A.B.R. 104-107** (opinion by referee), the claimant asserted a landlord's statutory lien.

The property came into possession of the bankruptcy court before the landlord took possession.

The landlord asserted a priority claim under the statutory lien, claiming that the possession taken by the trustee put the property in custodia legis and that such possession was for the benefit of the landlord as well as the creditors. The Court held:

> "But it would **violate** the main **purpose of the Bankruptcy Law** which is to distribute the property of the bankrupt equally among his creditors, to hold that the trustee represented lien claims, or would or could do anything to perfect or preserve a lien against his estate. Indeed, a creditor claiming a lien can do nothing to perfect it after proceedings in bankruptcy are commenced. If the lien is not then perfect the creditor is prevented from obtaining it. **Morgan v. Campbell, 22 Wallace, 381, sec. 67, Bankruptcy Act.**"

In the **Bindseil Case, 248 Fed. 112 (3rd Cir.)**, relied on by appellants, the Court said:

> "These cases hold in effect that until the mortgagee has reduced the mortgaged premises to his possession, or has attached or sequestered the rents (which, generally speaking, **cannot be done after bankruptcy**), the **possession** of the **trustee is that of the bankrupt mortgagor,** and rents from the mortgaged premises, which, but for bankruptcy, would belong to the mortgagor, after bankruptcy belong to the trustee by virtue of his title and possession, and are therefore applicable to debts due general creditors."

In **Industrial Finance Corp. v. Cappelmann, 284 Fed. 8 (4th Cir.), 49 Am. B.R. 525-530,** the Court held:

> "But there is no dissent from the view that the holder of an unrecorded mortgage or similar instrument who has not taken possession

before bankruptcy cannot recover the mortgaged property in the possession of the trustee, even when the state statutes protect only subsequent lien creditors, and not subsequent simple contract creditors, from an unrecorded instrument; for the reason that under the bankruptcy statute from the filing of the petition the trustee stands in the shoes of a subsequent lien creditor without notice."

Quotations from additional Federal decisions in bankruptcy cases, page 30 of this brief.

In re: Hotel St. James Co., 65 Fed. (2d) 82-84 (9th Cir.), the mortgage contained a provision authorizing the mortgagee to enter and take possession, to collect the rents and for the appointment of a receiver. The mortgagee did not take possession or have a receiver appointed prior to bankruptcy. The question as to the ownership of rents arose in the same manner as in the case at bar, to-wit: by petition to the bankruptcy court for an order requiring the trustee to turn over the rents. The Court sustaining the trustee's right to the rents, said:

> "In such circumstances the Second Circuit, In re Brose, 254 F. 664, has held that the mortgagee is not entitled to the money. After quoting . . . from Freedman's Saving & Trust Co. v. Shepherd, 127 U.S. 494:
>
> > 'The general rule is that the mortgagee is not entitled to the rents and profits of the mortgaged premises **until he takes actual possession**, or until possession is taken, in his behalf, by a receiver, ... or until, in proper form, he demands and is refused possession', the court continued: 'This general rule the federal courts will follow, except in cases where it appears that the **law of the state** where the premises are situated applies a different rule.'
>
> The court found that such was the rule in New York. So it is in California. 17 Cal. Jur. 288, page 1013; Freeman v. Campbell, 109 Cal. 360, 42 P. 35 (1895); Simpson v. Ferguson, 112 Cal.

180, 40 P. 104, 44 P. 484, 53 Am. St. Rep. 201 (1896), and a trust deed in California gives no greater right to possession, and thus rents, than does a mortgage."

In re Brose, 254 Fed. 664-666 (2nd Cir.), the controversy was between the trustee in bankruptcy of the owner and the receiver in a mortgage foreclosure proceeding instituted by a second mortgagee after bankruptcy. The second mortgagee petitioned the Bankruptcy Court for an order directing the bankruptcy receiver to pay the rents collected by him to the receiver in the foreclosure proceeding.

The Court held:

"There is no doubt what the general rule is relating to clauses in a mortgage giving the mortgagee the right to take the rents in terms similar to those used in the mortgage herein involved. It was stated by the Supreme Court in Freedman's Saving Co. v. Shepherd, 127 U.S. 494, 502 (1888), when Mr. Justice Harlan, writing for the court, said, citing cases:

(Quotation in Hotel St. James case.)

. . . . . .

The mortgage, the meaning of which is involved here, is a New York mortgage, and if the New York courts have determined its meaning this court must give the same meaning to its words which would be given to them by the courts of that State. . . . . .

The difficulty has been to determine what the law of that State upon the subject is. That difficulty has now been cleared up by a recent decision of the New York Court of Appeals in the case of Sullivan v. Rosson, 223 N.Y. 217, which reversed the decision made by the

Appellate Division to which reference has already been made, and upon which the district judge relied.

. . . . . .

The court in its opinion (referring to Sullivan v. Rosson), refers approvingly to the decision of the Supreme Court in Freedman's Case, supra. The case clearly settles the law of New York upon this subject, and establishes the principle that such a clause in a New York mortgage as is herein involved operates merely as a pledge of the rents, to which the pledgee does not become entitled until he asserts his right.

In view of that decision, this court holds that the receiver in bankruptcy herein is entitled to retain in his possession all rents due and collected by him prior to the time when the receiver appointed in the foreclosure proceedings acquired the right to possession of the premises by the entry of the order of his appointment on December 10, 1917."

In re: Humeston, 83 Fed. (2d) 187 (2nd Cir.), the owner of real property covered by a mortgage was adjudicated a bankrupt. A trustee was appointed to collect rents. Thereafter the trustee filed his account and gave notice of a hearing thereon. The mortgagee appeared and petitioned the Court that the rents collected be turned over to him. The Court held:

"We held in Re Brose, 254 Fed. 664, that when a mortgage contains an assignment of the rents, its effect as between a trustee in bankruptcy and a mortgagee depends upon the law of the situs. . . . . We treated this as settled law in **Re: Brose, supra, in Re McCrory Stores Corpora-**

tion, 73 F. (2d) 270, and in **Prudential Ins. Co. v. Liberdar Holding Corporation,** 74 F. (2d) 50, and we are not disposed to reopen the question. Obviously the mortgagee's position is worse when the mortgage does not assign the rents."

In **Willcox v. Goess, 92 Fed. (2d) 8, 12 (2nd Cir.),** the Court held:

". . . . . it is well settled in New York that a mortgagor may collect the rents—even when as here the mortgage assigns it—until the mortgagee has taken possession or got a receiver. (Sullivan v. Rosson, 223 N.Y. 217, 119 N.E. 405, 4 A.L.R. 1400; In re: Prudence Co., 88 F. (2d) 420 (C.C.A. 2)."

In **Alter v. Clark, 193 Fed. Rep. 153, 157 (Dist. Ct., Nevada),** the Court held:

"So long as Blaisdell and Wallace remained in possession of the property, they were entitled to apply its rents, issues, and profits to their own use. Their contract was to pay interest, not rent. When the trustee in bankruptcy took possession of the property, he took it 'with the title of the bankrupt', and with the same right to retain the rents prior to foreclosure, which the bankrupt had while they remained in possession. 1 Jones on Mortgages, Secs. 670, 771; Teal v. Walker, 111 U.S. 242, 4 Sup. Ct. 420, 23 L. ed. 415."

In **Smith v. D. A. Schulte, Inc., 91 Fed. (2d) 732 (2nd Cir.),** the Court held:

"The lessor, Schulco Company, Inc., mortgaged some of the parcels of land in question to the Central Hanover Bank & Trust Company, together 'with the right to receive all rents due

or to become due thereunder'. The debtor argues that this passed title to the rents out of the lessor. That is plainly untrue; the transfer was nothing more than a mortgage of future rents, and it is well settled in New York that until the mortgagee gets a foreclosure receiver, or the equivalent, the rents belong to the mortgagor." (Citing many cases.)

In 75 **A.L.R.** 1526, the Court will find an extensive annotation dealing with the precise question here involved under the title.

"Rights in respect of the rents and profits as between mortgagee and trustee in bankruptcy of mortgagor."

The annotator says:

"A conflict exists on the question here considered. **By the weight of authority** it is held that the mortgagor is entitled to rents and profits accruing up to the time the mortgagee enters, or brings a bill to foreclose or enter, and that **this right inheres in the mortgagor's trustee in bankruptcy**, and that the latter, up to the time the mortgagee takes action, takes the rents and profits for the benefit of the bankrupt's creditors."

In re: Israelson, 230 Fed. 1000 (U.S.D.C., N.Y.), the mortgage pledged the rents and provided for receivership on default. Suit to foreclose a mortgage was commenced in the State court after bankruptcy. A receiver was appointed in the foreclosure proceeding. He petitioned the court for an order requiring the trustee in bankruptcy to turn over rents collected by him.

The court held that the trustee in bankruptcy was entitled to the rents, and that,

> "The language used (referring to pledge of rents) . . . . . relates **only** to the rents **after** the entry and **taking possession** of the mortgaged premises."

Additional Authorities in support of appellees' contention that a pledge of rents does not create a lien until mortgagee obtains appointment of a receiver who collects rents.

In **Carlon v. Ruddle Properties,** 38 Pac. (2d) 149 **(Cal.),** a second mortgagee commenced foreclosure proceedings and obtained the appointment of a receiver who collected rents. The first mortgagee was made a party defendant who appeared and set up the priority of its mortgage, but did not seek to have the receivership extended for its benefit. Thereafter the first mortgagee commenced a separate foreclosure proceeding and prosecuted the same to foreclosure and sale, which resulted in a large deficiency judgment. The first mortgagee then applied to the Court that appointed the receiver for the rents in his possession. The Supreme Court of California held:

> "Later, in section 582 of the same volume, (Wiltsie, Mort. Foreclosure), pp. 753, 754, the author, citing Longdock Mills & Elev. Co. v. Alpen, 82 N. J. Eq. 190, 88 A. 623, says: 'If a receiver, pending a foreclosure action by a subsequent mortgagee, is appointed on his motion, and for his benefit, such an appointment enures to his benefit only; and where **no other lienholder** asked to have the receivership **extended to his lien,** the rents and profits should be applied to the discharge of his debt only. A junior mortgagee, obtaining the appointment of a receiver thereby acquires a specific lien on the rents collected by the receiver and is entitled to them as

against a prior mortgagee who made no application for the appointment of a receiver. The **junior mortgagee** is entitled to the rents collected, **even** though the prior mortgage contains a provision assigning the rents as further security upon default. The first mortgagee cannot have a deficiency judgment in his favor satisfied out of the funds collected by the receiver appointed at the instance of the second mortgagee.'

Again the author, in the same volume, section 622, page 795, quotes with approval the following from the case of Post v. Dorr, 4 Edw. Ch. (N.Y.) 412, 414: 'It was held "to be an established rule, that a second or third mortgagee who succeeds in getting a receiver appointed, becomes thereby entitled to the rents collected during the appointment, although a prior mortgagee steps in and obtains a receivership in his behalf and fails to obtain enough out of the property to pay his debt. This is on the principle that a mortgagee acquires a specific lien upon the rents by the appointment of a receiver of them; and if he be a second or third incumbrancer, the court will give him the benefit of his superior diligence over his senior, in respect to the rents which accrued during the time that the elder mortgagee took no measure to have the receivership extended to his suit and for his benefit".'

. . . . . .

Had no receivership been applied for, said rents, issues, and profits from the property would have inured to the benefit of the mortgagor and been wholly lost to both mortgagees. We therefore conclude that the petitioner has a special lien upon these funds, subject to the rights of the mortgagor, and respondent mortgagee is without any rights therein. These funds are the res or subject-matter of the foreclosure action

instituted by petitioner. Although, by a foreclosure of the senior mortgage, the property itself has been taken from under petitioner's lien, still said funds remain yet to be disposed of by a plenary judgment in the action, and respondent bank is without interest of any kind therein or in the judgment that may follow in the case."

In **Long v. W. P. Devereaux Co., 286 Pac. 402, 404, 405**, the Court held:

"(2) The mortgage in question here did not create a lien on the rents and profits, but simply conferred a right upon the mortgagee to impose a lien as additional security for the payment of the mortgage debt. Morton v. Union Central Life Ins. Co., 80 Mont. 593, 261 P. 278; Wells-Dickey Co. v. Embody, supra. . . . . .

(7) The prevailing rule is that if a mortgagee desires to avail himself of the right to rents and profit pledged by a mortgage upon real estate without the right of immediate possession of the land, he must claim them by invoking the aid of a court of equity for the appointment of a receiver to take possession of the rents and profits." (Citing a great many cases.)

In **95 A.L.R., p. 1053**, the Annotator says:

"It must be borne in mind, in connection with rents and profits of mortgaged land, that they are not a part of the land but only incidental thereto, and their impounding is not generally regarded as a matter of absolute right, but rather as a matter of remedy, to be resorted to only in aid of the ordinary remedy of foreclosure and sale. Under this view, the fact that one mortgage is senior or superior to another is not a predominant consideration; the important element is the invoking of the aid of the court to get at the profits of the land for the preserva-

tion of the mortgage security. Hence, it is argued that the mortgagee who first invokes the aid of the court in this respect obtains a superior right in the rents and profits thereby impounded, regardless of the seniority of his lien, at least until such time as the other mortgagee intervenes or commences a separate suit or otherwise asserts the superiority of his lien.

This line of reasoning has found expression in several well-considered statements."

In **Sims vs. Jamison, 67 Fed. (2d) 409 (9th Cir.),** (Appeal from an order made by Judge Fee) the Court dealt with a mortgage on crops to be grown in the future. The Court held:

"The rule applicable in the state of Oregon to a chatel mortgage upon **crops to be grown in the future** is stated as follows in U. S. Nat. Bank v. Wright, 131 Or. 518, 520, 283 P. 1, as follows:

'It is well settled that a chattel mortgage on crops to be thereafter sown and raised on the land of the mortgagor constitutes no lien on the land and will attach only to such interest as the mortgagor has in the crops **when they come into being.** Jones on Chattel Mortgages (5th ed.), Sec. 143a; Bouton v. Haggart, 6 Dak. 32, 50 N.W. 197; McMaster v. Emerson et al., 109 Iowa 284, 80 N.W. 389; Simmons v. Anderson, 44 Minn. 487, 47 N.W. 52; Collins v. Brown, 19 Idaho 360, 114 P. 671; Snerly v. Stacey et al., 174 Ark. 978, 298 S. W. 213, 214.'

See, also, Flanagan Bank v. Graham, 42 Or. 403, 71 P. 137, 790."

In **Re: West, 128 Fed. 205 (D.C. Oregon).** Several months prior to adjudication, the bankrupt assigned

future wages to secure a loan. The assignee claimed a lien on the wages subsequently earned. Judge Bellinger held:

> "The theory of a lien upon the earnings of future labor is not that it attaches to such earnings from the moment of contract of pledge or assignment, **but from the moment of their existence. It is needless to say that there can be no lien upon what does not exist.** . . . . If future earnings in such a case can be said to have a potential existence, they are the subject of an agreement for a lien; but the lien, or the so-called equitable interest, **does not attach until the wages come into existence, and until the lien does attach there is no lien.**

In **First Joint Stock Land Bank of Chicago v. Armstrong, 262 N.W. 815, 816,** the Court held:

> "It is well settled in this state by a long line of cases that **a pledge of rents and profits remote from the granting clause does not, in itself, create any lien upon such rents and profits.** (Cases.) It is equally well settled that such a clause does become effective and creates a chattel mortgage lien when the payments on the mortgage are in default **and action is brought to foreclose and for the appointment of a receiver.** (Cases.) It follows that where there are two mortgages covering the same property and containing such a clause, the **one which first starts action to foreclose obtains the first lien."**

In **Bank of America v. Bank of Amador Co., 28 Pac. (2d) 86 (Cal.),** a controversy between the holder of the real estate mortgage, including the crops, and the holder of subsequent chattel mortgage on the crops, the Court held:

"(6) In Casey v. Doherty, 116 Cal. App. 42, 2 P. (2d) 495, the rule is stated, supported by authorities cited, that 'a mortgagee not in possession is not entitled to the rents, issues and profits of the premises where the mortgagor has remained in possession of the mortgaged premises'. The fact that the rents, issues, and profits of the mortgaged property 'are expressly pledged for the security of the mortgage debt, with the right in the mortgagee to take possession upon default, the mortgagee is not entitled to the rents and profits until he takes **actual** possession, **or** until **possession is taken in his behalf by a receiver'**. . . . .

In the case of First National Bank of Lindsay v. Garner, 91 Cal. App. 176, 266 P. 849, this court went into the question very thoroughly as to the respective rights between a mortgagee whose mortgage included in its provisions, rents, issues, and profits, **as against a third person claiming under a chattel mortgage covering the crops** grown upon the mortgaged premises, and it was there held that, until the mortgage had been foreclosed, the mortgagor in possession was entitled to the rents, issues, and profits of the mortgaged premises, and of course possessed the right to mortgage the same."

In **Fisher v. Norman Apartments, Inc., et al., 72 Pac. (2d) 1092,** the mortgage (trust deed) contained a provision pledging and assigning the rents as security. After default an agreement was entered into between the owner and a bondholders' committee (mortgagee) by which a manager was appointed to operate the property, that the rents from the property were to be deposited in a "depository satisfactory to all parties herein" and were to be paid out only upon the joint signature of a resident manager

of the apartments and of a representative of the bondholders' committee for the purposes hereinafter set forth. Provision was made for the disposition of rents, first, to payment of operating expense, second, taxes and third, "to pay the balance, if any, to the trustee under said mortgage or deed of trust for the benefit of its bondholder beneficiaries. It was provided that the instrument should be construed as made for the benefit of the owner and of the bondholders' committee.

Foreclosure proceedings were instituted, and a decree of foreclosure was entered July 15, 1935. Sale was confirmed November 26, 1935, but prior to the sale, a **judgment creditor** of the owner **attached** by garnishment the rents in the possession of the depository bank, holding under the aforesaid agreement, and a controversy resulted between the mortgagee claiming the rents, both under the provision in the mortgage pledging and assigning the rents and also under the management agreement which provided for the payment of the rents to the mortgagee. The Court held:

> "The contract was a restriction on expenditures which might be made voluntarily by the manager or by the corporation, but it did not, and did not purport to, pass title to the funds or determine the rights of judgment creditors to proceed against them for satisfaction of their claims.
>
> (3) It is said that the rents were assigned in the deed of trust. This, however, does not operate to give the mortgagee a right to such rents

except under certain definite conditions. . . . Where rents are assigned to the mortgagee, a receiver may be appointed to take possession for him and collect the rents for his benefit; but this was not done. Neither under general principles of equity well recognized in foreclosure proceedings nor under our statute (if the same applies to prior mortgages which we need not determine) is the mortgagee entitled to the rent here involved.

. . . . . .

(7) The money in the hands of Englander, who, so far as the contract and record discloses, had no other status than that of agent of the Norman Apartments, Inc., was the money of his principal and subject to garnishment by a judgment creditor of his principal."